# PERSONAL SAVINGS AND DEBT MANAGEMENT

Quick Guide

**This Quick Guide was prepared by Truebridge**

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# Looking At Your Spending

Do you have enough money? Most people answer "no" when asked that question. You've probably seen the surveys... it doesn't seem to matter what your income is. Whether someone makes $30,000 or $300,000, all report that life would be much better if they just earned 10% more.

The secret to keeping more of your money lies in controlling your expenses. In order to accomplish that, you have to make a conscious effort to monitor where your money goes, take some time to examine your priorities and get your expenses in line with them.

That is the essence of financial planning: thinking and planning in the short term in order to prepare for a healthy financial future.

## Is Your Spending Out of Control?

Many people make statements such as the following (how many of them are statements you might make?):

- There's never any money left over at the end of the month.
- I don't have a budget.
- I am not sure how much I spend on basic items like food or clothing.
- I don't have nearly enough money in savings.
- I charge more on my credit cards than I pay off each month.
- My spouse and I fight about money all the time.
- I delay or avoid paying bills because there's no money.
- I worry about money constantly.
- If I could just hit the lottery, all my problems would be solved.
- I don't know how everybody else does it.

If four or more of these statements ring true, then your spending habits may need some serious scrutiny.

## Why Have I Gotten Into Debt?

If you ask somebody why he or she has gotten into debt, you may get answers like these:

1. I really don't know. I've just lost track of my spending.
2. Convenience. I'm always rushed, so I buy things that will save me time.
3. It is easy. The credit is there, so I use it.
4. There are lots of things I want, and I hate to deprive myself.
5. Everybody else does it. Why shouldn't I?
6. I've had one or more emergencies in the past year that have gotten me into financial trouble.
7. I can't stop spending.

If you would give some of these answers, it is time to think about the long term. What things will you be missing out on in the future because of the choices you're making now? A "yes" to number 6 means a focus on the short term. You need to get back on your feet. A "yes" to number 7 may mean that you need to deal with the issues that cause your behavior.

# Start with Planning

## Goals

Once you establish your priorities, or what's important to you, your next step is to come up with specific, written statements of your goals.

Sample goals:

- Accumulating emergency funds
- Getting out of debt
- Buying a house
- Taking a dream vacation
- Making improvements on a house you already own
- Financial independence
- Planning for retirement
- Sending the kids through college

Most people come up with goals like these and stop there. Don't make this mistake!

Be very specific about your goals. A goal is not really a goal until you have (1) a statement of the goal, (2) a time frame (when you need to pay for the goal) and

(3) a cost (how much the goal will cost you) attached to your statement.
Separate your goals into:

- Short-term: less than three years
- Intermediate-term: between three years and five years
- Long-term goals: more than five years.

Take a pencil and paper and write down the goals that come to mind. Let your mind wander. Involve your family in the process. Ask yourself which goals are wants and which are needs.

## The Need for an Emergency Fund

It is generally recommended that you have cash funds sufficient to cover three months of expenses. Some of these funds cover operating expenses, while the remaining serves as an emergency fund.

Ideally, the money you need should be in places that are easy to get to, e.g., bank and credit union savings accounts, and bank, credit union and money market accounts. These are liquid. You can turn them into dollar bills easily.

Although they are generally regarded as lower-risk, you should know that money market accounts are not federally insured (the way most banks are for deposits of up to $250,000).

If you don't have any cash reserves, here are some other sources of emergency funds:

- A home equity loan or line of credit (You should establish this now if you think you will need it in the future).
- Cashing in investments
- A loan on a margin account (if you own securities)
- A loan from a permanent insurance policy
- A personal loan from your bank or credit union
- A loan from your savings plan
- Credit cards (the LEAST favorable option)

## Calculate Your Net Worth

The next step is to find out where you are. You need to know exactly what you own (your assets), what you owe (your liabilities) and what, if anything, is left over (your net worth). This is called a net worth statement or balance sheet.

Take all the things you own - All the money you owe to others = Your net worth

Your net worth amount tells you how much wealth you have accumulated over the years. If you are disheartened by the figure, you're not alone. Many people want to throw up their hands and give up at this point. But stay with us! We are going to show you how to do something about it.

## Record Your Expenses

Now that you know how much you've accumulated, take a look at how you spend your money from day to day.

Most people do not have a good grasp of how much they spend. Items like rent or mortgage payments are easy to track. Other things, like electricity, fluctuate from month to month. And cash often falls into a deep dark hole known as "miscellaneous." Financial planners report that their typical client doesn't know where 5 to 15% of disposable income (take-home pay) is spent.

Think about that: 5 to 15% could mean the difference between falling into debt and meeting your financial goals.

- A few points on how to fill in the Worksheet:
- If you withdraw $100 out of the cash machine, don't put that in. Put what you spend it on.
- Enter items when you put them on the charge card, not when the charge comes in.
- Put a star or asterisk beside items that do not occur regularly. Car or home repairs fall into this category.
- This worksheet will help you keep track of your expenses over the next few months.

## Bring Your Family into the Picture

If money means security to you, and pleasure to your spouse, then you are going to be a saver and your spouse will want to spend. Such differences can cause huge conflicts. Communication and compromise are the keys, and when you talk, it's important to do it at a time when emotions aren't running high.

If you have children, and they're old enough to understand, consider bringing them into the discussion as well—not to the point of scaring them, but to let them know what's going on. Helping them to understand the principles of money management early in their lives could be doing them a big favor.

## Income and Expenses

To be successful in managing your cash flow and debts, you need to have an accurate picture of both your income and your expenses.

***Income***

Income is any money you receive. Taxable income includes wages, alimony, certain interest dividends, rental income, commission and tips, unemployment compensation, capital gains, pension, annuities, Social Security and royalties. Non-taxable income includes child support, gifts, and inheritances.

***Expenses***

Expenses are more varied, ranging from obvious items such as mortgage (or rent) and food, to items that you might not normally keep track of, such as home repair, grooming and entertainment.

To get the necessary clear picture, you will need to figure out your paycheck and track your expenses line by line.

## Constructing a Spending Plan

Once you've thought about your goals and priorities, examined your attitude towards money, put together a balance sheet, and done a cash flow analysis, your next step is to take all you've learned and put together a spending plan that works for you.

You have a certain amount of money available to you. You can spend it any way you choose. What are the choices that are best for you? How do you plan your spending so that it is in line with your goals and priorities?

***Time Frame***

Think about how to build your plan. For most people, a plan built around their pay period may work best. It could be weekly, or every two weeks, or twice a month, or monthly. If you have two incomes with two different time frames, then it usually works best to center the plan around the larger check.

***Fixed and Variable Expenses***

Payments you are committed to, such as taxes, rent, mortgage payments, loan payments and insurance, are called *fixed expenses*. In reality, however, few expenses are set in stone. You can move to a cheaper apartment or sell your house and buy one that's less expensive. You can raise the deductible on your insurance.

Expenses you have significant control over or which change from month to month are called *variable expenses*. These are things such as food (you can avoid eating out), utilities (turn off the lights), clothing (wear it out) and gasoline (carpool).

> **SUGGESTION**: Focus on variable expenses first when you are developing your spending plan.

The first questions to ask:

- Do you pay yourself first? Do you set aside money for savings first, and spend what's left? That's the best approach to a spending plan.
- How much of your money is spent on convenience foods and eating out?
- Do you buy your clothes at outlets, wait for sales, or do you pay full retail prices? Do you need all the clothes you buy?
- Can you save money on vacations by swapping houses with someone or staying local?
- Can you live without premium cable or satellite TV?
- If you have a recreational activity you regularly pursue, can you do it at off-peak times?

The choices are up to you. It all depends on what you are trying to achieve. If eating out is your favorite thing in life, you should find a way to afford it. If you love clothes, make them a priority. The point is to find out what it is you really want, and focus your resources there. Reduce or eliminate the things that don't mean as much.

Go back to your expense record again. How many of the things you bought were worth it? Aren't there items on that list you can't even remember buying? Or look at your bank statement and try to remember where all the dollars went that you took out of the cash machine. If you don't know, chances are those things weren't that important to you.

# Should I Borrow Money?

Borrowing money can be a useful way for you to achieve specific goals. However, there may be alternatives to borrowing that give you better results.

*Savings*. Look here first. Of course, it is not wise to tap into your emergency fund, but if there is extra cash, you will want to look at this option before borrowing.

*Selling assets.* Selling shares of stock, or perhaps a piece of property that you inherited, could make better financial sense than borrowing. Don't misunderstand—we are not advocating that you hock your valued possessions. What's more, the value of your possessions may have been slashed by the market crash and the recession, and waiting for their value to rebound may be a better alternative than selling them at a steep loss. But selling an asset before you borrow money is at least worth evaluating.

## Think Before You Borrow - Key Considerations

It is important that you go through a series of steps before deciding if you should borrow money. Here are the steps:

- Look at all the options available to you. What's least expensive? Using money in a savings account? Selling an investment? Or borrowing the money?
- Can you afford it? What does your current loan situation (including credit cards) look like? If you are already heavily in debt, you may want to reconsider borrowing and wait until you are in better financial shape.
- Consider potential tax benefits. If the interest you pay is tax-deductible, it reduces the net cost of borrowing. The IRS disallows almost every type of interest expense deduction, except for some interest on home loans, investment interest expense and possibly some interest on student loans. So, if you are a homeowner with equity in your home, there may be a tax benefit associated with mortgages and home-equity loans.
- Evaluate your attitude towards borrowing. Learn to use debt wisely. You shouldn't go into debt to live for today and then pay tomorrow. However, it doesn't make sense to avoid debt entirely. If your borrowing cost is 4% and you can earn 6% on your investments, it could make sense for you. When used wisely, borrowing can be a useful tool to reach your financial goals.

## Where Should I Borrow?

Once you decide to borrow, look at the different sources of cash that are available to you.

- If you are a homeowner with equity in your home, there are some attractive ways to use the equity in your home as a means of getting cash.
- If you are not a homeowner or have no equity in your home, you still have several different options to consider, such as borrowing from a retirement plan or insurance plan, or taking out a personal loan.
- It may be that you can easily borrow from family members.

# Managing Your Credit

## Racking Up Debt

Although credit can be harder to come by these days, it is still extremely easy to get into debt. Furniture companies and car dealers still offer deals that involve little or no down payment and let you pay off the debt over long periods. Tempting credit card offers still appear regularly in your mailbox.

In some ways, easy credit is good. If you're starting out or starting over, credit can put a roof over your head and bread on the table and give you time to get on your feet. And, for people who are very disciplined, credit can be a way of keeping track of expenses. Some people put almost every penny they spend on credit cards, so they will have an itemized list each month of exactly where their money went.

But many people aren't that disciplined. For them, credit is a way of having things now instead of later. That's fine if there's enough money later to pay for the things. But if there isn't, that means mounting bills, credit card balances, and big-time debt.

## How much debt is too much?

Take the following quiz to see if debt is a problem for you.

1. Is your savings cushion inadequate or nonexistent?
2. Are you using credit cards for items you used to buy with cash?
3. Are you at or nearing the limit on your credit cards?
4. Are you unsure about how much you owe?
5. Is an increasing percentage of your monthly income going to pay off debts?
6. Are you able to make only the minimum payments on your credit cards?
7. If you lost your job, would you be in immediate financial difficulty?



If you answered yes to two or more of these questions, you need to take a long, hard look at your finances.

## Getting Credit

A credit report is a summary of your credit history. You should take a look at yours, especially if you have problems with debt.

Our "cashless society" makes having available credit absolutely necessary.

How much credit you get will depend largely on what your credit report says. The information on it will determine your credit rating. The first step in managing your credit is to understand the possible reasons for being denied credit. It is also important to understand how to safely use your credit card for Internet purchases.

Even if you have a poor credit history or have declared bankruptcy, there are things you can do to reestablish credit. You also have certain rights if you are approached by a collection agency. And you may benefit from the services of a credit counseling agency.

## Reasons for Being Denied Credit

There are a number of reasons for being denied credit, such as a history of paying late or slowly, having had collection procedures initiated against you, or having filed for bankruptcy. Having too many credit cards can be another. Even if you don't use the cards, they represent credit that's available to you. If that credit becomes too high a percentage of your salary, no one will want to loan you money. A creditor may even refuse you credit if you've had too many credit inquiries over the past few months, because that may mean you've got multiple applications for credit being applied for simultaneously.

Another problem is credit fraud. It is all too easy for unscrupulous people to get access to your personal information, which can then be used to apply for credit in your name. If you find that you are getting bills for things you didn't buy, take action immediately! The sooner credit fraud is discovered, the sooner you can start to make repairs to your credit rating.

## Reestablishing Credit

Reestablishing credit can be tough to do if you have a poor credit history or have declared bankruptcy. The bankruptcy filing remains on your credit record for up to ten years, and creditors obviously shy away from people with a bankruptcy record or a bad credit history.

Here are some basic steps you can take to start the process of reestablishing your credit.

- When you've built up savings in your bank savings account, take a "passbook" loan. The account will be frozen for the amount that you have borrowed. Repay the loan on schedule and this will demonstrate your willingness to be responsible about your debt.

- Have a loan co-signed by a family member or friend. Remember, though, if you can't make the payments, he or she will be liable for the balance.

- Get a debit card, which looks and acts like a credit card, except that it takes money right out of your checking account. Some financial institutions will issue that to you as a "first step" on the way to a regular credit card.

- Get a department store charge card. These are generally much easier to get than Visa or MasterCard. But be sure to make your payments on time!
- DON'T pay a "credit agency" money to have your credit reestablished. They can charge high fees, and rarely do more for you than you can do for yourself.

You'll need to be patient in order to reestablish credit. It will take time.

## Talk to Your Creditors

When you are having financial difficulties, it is always a good idea to contact your creditors. And if you know you're heading for hard times (you're being laid-off or are about to be treated for an illness), contact your creditors in advance to let them know.

Your creditors don't want to call and harass you or take you to court. These actions are expensive and time-consuming for them. They simply want their money. If you can give them reasonable assurances that they will get their money eventually, they will usually try to work with you.

There are many kinds of arrangements your creditors can make. They can defer your payments for a few months, if your problems are short-term. (The interest will still accrue, though.) They can restructure your debt, so that you pay a smaller amount each month over a longer period of time. If your creditor is a bank, they may even be able to make some suggestions about debt consolidation or restructuring.

**SUGGESTION**: If you reach an agreement with your creditors, get it in writing! It is very difficult to prove that an oral agreement exists.

## Collection Agencies

If you have serious credit problems, you may be past the talking stage. A collection agency may already be at your door. You should know that you have a number of rights in this situation, under the Fair Debt Collection Practices Act.

- Collectors may not harass or abuse you.
- Collectors may not lie to you or use false statements.
- Collectors may not engage in unfair practices.
- They are not permitted to contact you at unreasonable hours, unless you agree to be contacted at those times.
- They must send you a written notice telling you the amount you owe.
- If you send collectors a written denial of the debt, they may not contact you until they provide you with proof of the debt.
- If you have an attorney, the collection agency cannot contact anyone other than the attorney to obtain information about you.
- Collectors do have the right to contact you, at reasonable hours, by mail, telephone, telegram, or fax.
- If a collector has violated the law, you have the right to sue. The lawsuit must commence within one year of the cause for action.

You can report troubles with collectors to the Attorney General's office in your state, or to the Federal Trade Commission in Washington, DC.

## Credit Counseling

If you feel like you need some help dealing with credit issues, you can talk to a credit counselor. This is a specially trained person who will help you with your cash flow and intervene with your creditors.

The Consumer Credit Counseling Service (CCCS) is a not-for-profit agency that provides credit counseling. Contact the National Foundation for Credit Counseling (NFCC) toll-free at 1-800-388-2227, or on-line at www.nfcc.org, to locate a local CCCS office.

Some credit counselors are not what they seem. Before you pick one, ask how they are compensated. They may want to charge you large fees, yet be of limited help. Check with the Better Business Bureau in your area, or ask your bank for a referral. ♦