

Your Money Cheat Sheet

The best financial advice tends to apply to pretty much everyone. You don't need a spreadsheet of pros and cons and complex scenarios. What you need is a rule of thumb.

There's no shame in using one-size-fits-all advice. A study of West Point cadets, for example, found teaching rules of thumb was at least as effective as standard personal finance training in increasing students' knowledge and confidence as well as their willingness to take financial risks. Researchers found money rules of thumb were more effective than teaching accounting principles to small-business owners in the Dominican Republic.

Here are a dozen shamelessly simple money rules of thumb I've collected over the years. (These address how you borrow and save. If you just want to know how you're doing with money, we've got a quick way to [score your financial health](#), too.)

1. Build up emergency savings

You need to be able to get your hands on cash or credit equal to three months' worth of expenses. The classic [emergency fund advice](#) — that you need three to six months of expenses saved — is great, but it can take years to save that much and you have other more important priorities (see “retirement,” below). While you build up your cash stash, make sure you have a Plan B for a true emergency. That could be money in a Roth IRA (you can pull out your contributions at any time without paying taxes or penalties), space on your credit cards or an unused home equity line of credit.

2. Save 15% for retirement...

If you got a late start or want to retire early, you may need to save more. [Run the numbers on your retirement plan](#). For most people, 15% including any company match is a good place to start. Even if you can't save as much as you should, start somewhere and kick up your savings rate regularly. Retirement should be your top financial priority. You can't get back lost company matches, lost tax breaks and the lost years when your money isn't earning tax-deferred returns.

3. ...and don't touch that money

Leave retirement money for retirement. When your retirement fund is small, you may feel like spending it doesn't really matter. It does. Taxes and penalties will cost you at least 25% and likely more of what you withdraw. Plus, every \$1 you take out costs you \$10 to \$20 in lost future retirement income. Once your retirement fund is larger, it may be easy to convince yourself there are good reasons to borrow or withdraw the money. There really aren't. Leave the money alone so it's there when you need it. (See “[How to Write a Retirement Plan](#).”)

4. Save for college

Get in the habit of putting at least \$25 a month aside for college soon as your child is born. Even small contributions to a [529 college savings plan](#) can add up over time — perhaps the difference between choosing the best school and choosing a school based on its financial aid package. (But if you have to choose, retirement saving is more important. Your kids can always get student loans, but as you've probably heard, no one will lend you money for retirement.)

5. Plan and manage your student loans

Your total borrowing shouldn't exceed what you expect to make your first year out of school. At today's interest rates, this will ensure that you can pay off what you owe within 10 years while keeping payments below 10% of your income, which is considered an affordable repayment rate. What if you didn't limit your borrowing and are now struggling? You have options. (See "[Find the Best Student Loan Repayment Plan.](#)")

6. Cars: Buy used and drive it for 10 years

New cars are lovely, but they're expensive and lose an astonishing amount of value in their first two years. Let someone else pay for that depreciation and take advantage of the fact that today's better-built cars can run well for at least a decade if properly maintained. You can save hundreds of thousands of dollars over your driving lifetime this way. (See "[How to Buy a Used Car.](#)")

7. Car loans: Use the 20/4/10 rule

Ideally, you wouldn't borrow money to buy an asset that loses value, but you may not always be able to pay cash for a car. If you can't, protect yourself from overspending by putting 20% down, limiting the loan to four years and capping your monthly payment at no more than 10% of your gross income. A big down payment keeps you from being "underwater," or owing more on the car than it's worth, as soon as you drive off the lot. Limiting the length of the loan helps you build equity faster and reduces the overall interest you pay. Finally, capping the size of the payments prevents your car from eating your budget. (See "[How to Build a Budget.](#)")

8. Make credit cards work for you

If you carry a balance, look for a low-rate card so you can pay off your debt faster and don't mess with rewards cards right now. If you pay in full each month (as you should), find a rewards card that returns at least 1.5% of what you spend. You should regularly review your rewards programs to make sure you're getting enough value from them. The programs can change, as can your spending and the way you use rewards. (For a "lazy optimizer" approach, check out "[Sean Talks Credit: How I Maximize My Rewards with Only a Few Credit Cards.](#)")

9. Square away your insurance

Cover yourself for catastrophic expenses, not the stuff you can pay out of pocket. Insurance should [protect you against the big things](#) — unexpected expenses that could wipe you out financially, such as your home burning down or a car accident that triggers a lawsuit. You want high limits on your policies — and high deductibles, too. Small claims don't make financial sense in the long run. You may gain some small insurance payments, but you risk a rate increase that could more than cancel out your gains.

10. Choose a reasonable mortgage amount

If you can't afford the payment on a 30-year, fixed-rate mortgage, you can't afford the house. You may be able to save money by using another kind of mortgage, such as a hybrid loan that offers a lower initial rate. But if you're using an alternative loan because that's the only way you can buy the home you want, you may have set your sights too high. A budget-busting mortgage puts you at risk of spiraling into ever-deeper debt, especially when you add in all the other costs of homeownership. (Read "[The Huge, Hidden Costs of Owning a Home.](#)")

11. Choose the right mortgage rate

Fix the rate for at least as long as you plan to be in the home. Plans can change, obviously, but you don't want a big payment jump to force you out of a home you hoped to live in for years to come. If you're pretty sure you'll be moving in five years, a five-year hybrid could be a good option. If you think you may stay for 10 years or more, though, consider opting for the certainty of a 30-year fixed rate. ([Compare rates on different types of mortgages.](#))

12. Back-burner those mortgage prepayments

You have better things to do with your money than prepay a low-rate, potentially tax-deductible mortgage. Shaving years off your mortgage and saving money on interest sounds great. But before you consider making extra payments to reduce your mortgage principal, make sure more important priorities are covered. You should be saving enough for retirement. You should have paid off all other debt, since most other loans have higher rates and the interest isn't deductible. It would be smart to have that emergency fund built up as well and to be adequately insured. If you've covered all of those bases and still want to pay down your mortgage, have at it.

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