ON THE MONEY

A Young Person's Guide to Personal Finance

Budgets
Banking • Credit
Insurance • Investing
Debt Collection & More!

State of Maine Bureau of Consumer Credit Protection
Department of Professional and Financial Regulation

DEPARTMENT OF
Professional &
Financial Regulation
STATE OF MAINE

- OFFICE OF SECURITIES
- BUREAU OF INSURANCE
- CONSUMER CREDIT PROTECTION
- BUREAU OF FINANCIAL INSTITUTIONS
- OFFICE OF PROF. AND OCC. REGULATION

Downeaster Common Sense Guide

On The Money: A Young Person's Guide to Personal Finance

By David Leach, MPA, and Kyrie Johnson

Paul R. LePage
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Maine Bureau of Consumer Credit Protection

Toll-free Maine Consumer Assistance	Maine Foreclosure Prevention Hotline
1-800-332-8529 (1-800-DEBT-LAW)	1-888-NO-4-CLŌZ
TTY users call Maine relay 711	(1-888-664-2569)

www.Credit.Maine.gov

The Maine Bureau of Consumer Credit Protection was established in 1975 to enforce a wide variety of consumer financial protection laws, including:

- Consumer Credit Code
- Truth-in-Lending Act
- Fair Credit Billing Act
- Truth-in-Leasing Act
- Fair Credit Reporting Act
- Fair Debt Collection Practices Act
- "Plain Language" Contract Law

The Bureau conducts periodic examinations of creditors to determine compliance with these laws, responds to consumer complaints and inquiries, and operates the state's foreclosure prevention hotline and housing counselor referral program. The Bureau also conducts educational seminars and provides speakers to advise consumers and creditors of their legal rights and responsibilities.

William N. Lund, Superintendent
December 2016

DOWNEASTER COMMON SENSE GUIDE
ON THE MONEY: A YOUNG PERSON'S GUIDE TO PERSONAL FINANCE

By David Leach, MPA and Kyrie Johnson
Editing and Production: Steven Lemieux, MBA

Maine residents can obtain additional free copies of this booklet by contacting the Bureau of Consumer Credit Protection at 207-624-8527 or toll-free at 1-800-332-8529. Non-Maine residents may purchase the publication for $6 per copy, or at a volume discount of $4 per copy on orders of 50 or more. Shipping fees are included in the prices listed.

Dear Reader,

"The Greatest Generation" is a phrase made popular by retired NBC News anchor Tom Brokaw when referring to the American women and men who helped achieve victory in World War II.

You have a chance to be remarkable too — as a generation that possesses the power and control to shape your future through sound financial literacy knowledge combined with personal money management best practices.

A common conversation across America each day is that young people are not provided with the fundamental knowledge they need to form basic personal financial skills. This booklet is a "game changer" in that discussion, and is written just for you!

Within the covers of this guide you will find factual, unbiased information on the following essential money topics:

- Money Management Skills and Strategies
- Bank/Credit Union Accounts (Checking, Savings, CDs, etc.)
- Consumer Credit & Responsible Borrowing
- Insurance Products (Life, Health, Auto, Home, Disability, Annuities)
- Investment and Building Your Portfolio (Stocks, Mutual Funds, Bonds)
- Recognizing and Fighting Back Against Financial Scams

We hope the knowledge and skills you gain by reading this guide will help make your adult life a great success and make you a part of the greatest financial generation!

Sincerely,

David Leach, MPA	Kyrie Johnson
Principal Examiner	Margaret Chase Smith Summer Intern, 2016

Special Thanks to our Contributors

The following agencies provided valuable information for this booklet: Maine Bureau of Financial Institutions, Maine Bureau of Insurance, Maine Office of Securities, Office of MaineCare Services, University of Maine at Augusta, Maine State Treasurer's Office, and the Finance Authority of Maine (FAME)

Table of Contents

I. Setting a Budget

The average American earns more than $1,000,000 during their lifetime (assuming you work 40 years with minimum average yearly earnings of $25,000 or greater[1]). The average American is also $37,364 in debt.[2,3] Your first few years in the workforce can set the tone, financially, for the rest of your career.[4] What can you do to make your money work for you?

Saving

Saving early in life can have a big impact on your finances later on. Being young is your greatest advantage when it comes to building an impressive nest egg. If you set aside $100 at 6% **annual percentage yield ("APY")** each month starting when you turn 18, you will have $227,016 by the time you turn 60. If you wait seven years and start at age 25, you'll only have $142,471 by the time you turn 60 — an $84,545 difference!

Save early, and save often. Set a savings goal, or set a percentage of your income aside — maybe 10-20% of your **gross** (pre-tax) earnings. Have the funds automatically deducted from your paycheck and direct deposited into savings accounts, investment accounts, retirement accounts (*e.g.,* 401K), bank certificates of deposit ("CDs"), or some combination of the above.

Unexpected events, like illness, unemployment, or accidents, can cause serious money problems. You need a cushion! Before you spend money left over after required expenses and savings, put an additional 10-20% of your take-home pay in a separate account. Keep doing so until you have an amount equal to either 10% of your annual income or three to six months of required expenses — whichever is greater. This is your emergency fund (a/k/a "rainy day fund"). Leave it in the account. Don't touch it unless you have no other choice. It will be there if you need it, and you'll be thankful to have it.

Solving Money Problems

Not all money problems come out of the blue. Some warning signs include having trouble paying bills on time, being consistently

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[1] U.S. Bureau of Labor Statistics. (2016). [Graph illustration of U.S. Bureau of Labor Statistics Current Population Survey]. *Earnings and unemployment rates by educational attainment, 2015*. Retrieved from http://www.bls.gov/emp/ep_chart_001.htm

[2] U.S. Census Bureau. (2016). *Monthly population estimates for the United States: April 1, 2010 to December 1, 2016*. Retrieved from http://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?src=bkmk

[3] El Issa, E. (2016). *2015 American Household Credit Card Debt Study*. Retrieved from https://www.nerdwallet.com/blog/credit-card-data/average-credit-card-debt-household/

[4] Guvenen, F., Karahan, F., Ozkan, S., & Song, J. (2015). *What do data on millions of U.S. workers reveal about life-cycle earnings risk?* (Federal Reserve Bank of New York Staff Reports No. 710). Retrieved from https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr710.pdf

overdrawn at the bank, or needing to borrow money for things you used to pay cash for. Most problems, including money problems, can be solved in four steps:

1. Identify the problem. You can't solve a problem until you know what the problem is. A cash shortage could be a sign something else is going on. What's the root cause of your money problems? Low income? Unexpected illness? Emotional attachment to something you can't really afford? Uncontrolled spending?

2. Design solutions. There's more than one solution to every problem. What are your options? Don't be afraid to ask friends or family for ideas. Common solutions to financial problems include:

- Lowering expenses. Turn down the heat. Stockpile non-perishable groceries when they're on sale. Bring your lunch to work from home instead of eating out. Small changes to your spending habits can add up.

- Spending only cash. Withdraw your spending money from your bank account once each week, and don't go back until the next week. It will help you develop financial discipline, limit how much you spend, and increase your spending awareness.

- Downsizing. Can your needs be met with a smaller, less expensive home, vehicle or lifestyle?

(continued on next page) →

The Perfect Budget?

One of the hardest things to figure out when you set up a budget for the first time is how much you should spend on different types of expenses. There is no single perfect budget. Every household is different. Every family is different. If you're not sure how to allocate your money, use these guidelines from the Federal Reserve Bank of Boston's New England Consumer Advisory Group as a starting point:

1. **Housing (35%)** - Rent/mortgage, utilities, maintenance, taxes and insurance.
2. **Transportation (15%)** - Car loan, gas, parking and upkeep...public transportation.
3. **Other Debt Repayment (15%)** - Not your mortgage or car loan[s], but student loans, credit cards and other debts.
4. **Savings/Emergency (10%)** - No questions asked. Non-negotiable.
5. **Life (25%)** - Everything else: clothing, travel, healthcare, fun.

You can change these percentages, but be sure they add up to 100%! You can also borrow from one category to another, except for savings.[5]

[5] New England Consumer Advisory Group. (2010). *The Consumer Financial Emergency Survival Guide.* Boston, MA: Federal Reserve Bank of Boston.

3. Choose your solution(s). No solution is 100% right or wrong. Consider your options. What financial solution or combination of solutions will work best for your situation?

4. Implement your financial solution. Even the best solution is worthless if you can't put it in place. Once you've decided how to tackle your money problems, stick with it. Keep an eye on your performance. Are your solutions working? If not, you may need to reassess your situation. Would another solution work better? Or is there another problem you need to address?

The Five Steps to a Successful Budget

One of the best ways to keep yourself out of financial trouble is to create a budget. There are five steps to a successful budget.

1. A successful budget starts with a goal. What's important to you? Do you want to buy a car? Go to college? Decide what you want, and go after it. Set clear, realistic goals. Write them down. How much money do you need to achieve your goals? When do you want to reach them? Goal setting is your responsibility. Your future is in your hands.

2. Everyone's budget is different, but all budgets come down to a simple formula: **income - expenses = savings.** Start by identifying your income. Where does your money come from? Write down everything: wages, tax benefits, support from your family, interest income, investment income, and anything else.

   Identify your expenses. Ask yourself, "Where am I spending my money?" Keep track for a few weeks. Record everything you spend money on. You might be tempted to only write down items you *think* you should have in your budget. Resist the urge. If you don't identify your expenses, your budget won't be accurate. If you're not already tracking expenses, you may be surprised to see where your money is going.

   Most people's expenses aren't all on the same schedule. Before you can make a

Budgeting with Irregular Income

You can't always count on a steady paycheck. Lots of people rely on sales commissions, tips, seasonal work, or other irregular sources of income. If you don't have a steady flow of funds, you can still put together an effective budget. You may just need to adjust your approach.

Try figuring out your average income over a long period of time (*i.e.,* a year). Divide your average yearly income by 12, and create a monthly budget based on that amount. You might also consider putting together multiple budgets: a budget for good months, and a budget for months when money is tight.

plan, you need to sync everything up. If you have weekly expenses, multiply the amount by four to find the total for the month. If you have bi-weekly expenses, multiply by two. If you have a bi-monthly expense (every two months), divide by two. If you have a yearly expense (*e.g.*, car registration), divide by 12.

3. Expenses fall into two categories: needs and wants. One of the most important steps to a successful budget is separating the two. It's not always easy. Not everything you feel is a need is actually a need. Ask yourself, "Is this something I could do without?" Consider the essentials, like food, shelter, and reliable transportation. There are different ways to fulfill your needs. You *need* basic groceries to survive; you *don't need* to eat out. See "Needs vs. Wants," below, to help you sort. Think critically. Your choices will determine whether you reach your goals. Financing a $40,000 pick-up truck on an annual salary of under $30,000 simply does not make sense to a careful budgeter.

4. Compare your income and expenses. How much are you spending now? How much do you *need* to spend each month to keep yourself afloat? Make sure your expenses aren't greater than your income. Evaluate your budget. Ask yourself, "Will this budget help me reach my goals?" At this point, you should have a workable budget. Double-check it. Are there any errors or items unaccounted for?

5. It's time to put your budget plan into action. We've created a *monthly* budget. You may be paid on a different timetable. Match your spending to your income

Needs vs. Wants

A need is something you can't do without. A want is something you would like to have. Most people need only five things: food and water, shelter, and basic healthcare, hygiene products, and clothing. It's important to separate needs and wants when you're creating a budget. Although they may not be necessary for survival, needs factored into your budget should also include any required expenses, such as utilities, basic transportation, and bills. Use the examples below to help you separate your needs from your wants.

Needs

- Basic groceries
- Basic clothing
- Basic transportation (*e.g.*, bus fare, fuel)
- Housing expenses (*e.g.*, mortgage; rent)
- Insurance
- Utilities
- Taxes

Wants

- Eating out
- Entertainment
- Non-basic clothing
- Media (*e.g.,* books, TV, and movies)
- Recreational Travel
- Gym/Club Memberships
- "Pocket money"

schedule. If you're paid bi-weekly, align your spending to a two-week schedule. If you've included seasonal or annual expenses in your budget, figure out how much money you need to set aside each paycheck to cover those expenses. It may be a good idea to deposit this money in a separate account until you need it.

<u>Living paycheck to paycheck is no way to get ahead</u>. It's like skating on thin ice. You may think you're fine, but you could be in deep trouble at any moment. Many successful people practice **defensive spending**: spending less than they have, and watching every dollar. Defensive spenders have funds left over after most pay cycles. They save and invest that money, growing their nest eggs for a financially successful working life and retirement. You worked hard for your money. Use it wisely!

Thinking Critically

Critical thinking is the process of objectively evaluating information, often to make a decision or solve a problem. Critical thinkers need to make detailed observations, <u>separate fact from opinion</u>, and make sound decisions based on evidence and logic. It can take time to develop critical thinking skills. Don't expect to master them overnight. Maintain doubt and suspend judgement; don't jump to conclusions. Always evaluate <u>all</u> your options.

Critical thinking isn't always pleasant, but it's a powerful tool for making financial decisions. Ask yourself a few questions about your finances, and think critically about the answers:

- What was the last item you purchased that you regret buying? Why did you regret it? How can you avoid making the same mistake again? We all make mistakes; just don't keep making the same ones!
- How much are you actually making each week when you take into account your required expenses? What can you do to increase your income or reduce your costs?
- Where do you want to be financially one year from today? How about five years from today? How do you get there? At what age do you want to retire?

II. How "Interest" Works

There's no such thing as free money. Lenders expect to be repaid, with **interest**. To a lender, interest (expressed as **annual percentage rates**) is the amount charged in excess of the original **principal** balance of a loan, which is the money borrowed. Interest is the difference between the principal and the sum of all payments made. Deposit-taking financial institutions pay interest (expressed as **annual percentage yields**) to depositors. Depending on the business and type of product, interest could be calculated a few different ways.

Simple Interest

Simple interest is based only on the original principal balance of the loan. The formula for simple interest is, well, simple:

$$I = P \times R \times T$$

"I" is the total interest earned, in dollars. "P" is the amount borrowed. "R" is the interest rate. "T" is the time elapsed between the date of the transaction, and **maturity** — the date the loan is due. The "time" part of the simple interest formula is especially important. In a simple interest calculation, time is expressed as a number of units of time. A unit could be day. It could be four days. It could be a week, a month, a year, or even more. If you borrowed $100 at an interest rate of 5% *per year*, in one year's time you would owe $5 interest. If you borrowed $100 at a rate of 5% *per month* for one year, in one year's time you would owe $60 interest.

Compound Interest

Interest isn't always simple. **Compound interest** is charged on both the principal balance and on interest that has already accumulated. The formula for compound interest looks something like this:

$$FV=PV(1+r)^N$$

"FV" is the future value of the loan balance or deposit: the sum of the principal amount and all interest accumulated over the lifetime of the loan or deposit. "PV" is the present value: the original or current principal balance. "r" is the interest rate. "N" is the number of compounding periods.

If you deposited $100 at an annual interest rate of 5% for one year, at the end of that year you would receive $5 interest. If you deposited that $5 and left the original $100 in your account for a second year, you would receive an additional $5.25 in interest (for a total of

"A rich man is nothing but a poor man with money" –W.C. Fields

$10.25 interest) — $5 on the principal balance during the second year, and $0.25 on the interest that accumulated during the first year ($\$110.25=\$100(1+.05)^2$). Compound interest can be a powerful tool for saving (see chart, below).

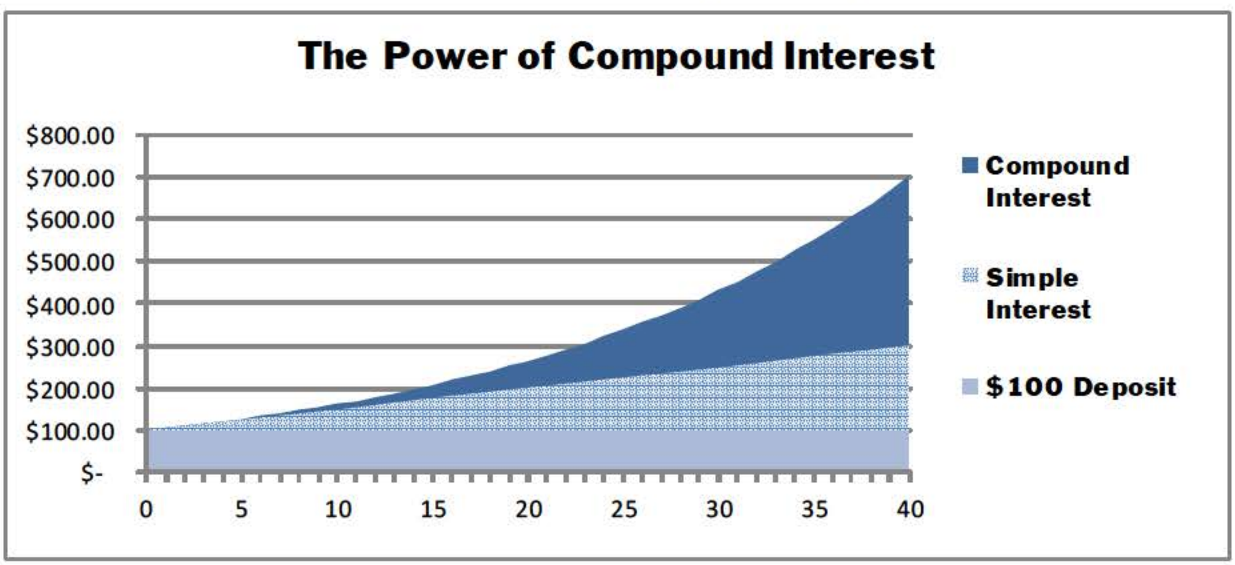
Fixed vs. Variable Rates

Many transactions feature **fixed interest rates**: rates that don't change for the term of the transaction, no matter what happens to the market. Not all transactions are like this. Some feature **variable interest rates:** rates that rise or fall periodically as market rates change.

Fixed rate transactions generally start off with higher interest rates than variable rate transactions. Since the rates on fixed-rate loans can't change, payments stay the same from **disbursement** until the repayment period ends. If rates fall, a fixed rate will remain higher than a variable rate. Since variable rate loans feature rates that can change, required payment amounts may vary over time. If market rates rise, the interest rate and payments may be higher than rates and payments on a fixed-rate loan.

Everyone's situation is different. There's no one right answer when it comes to choosing between fixed and variable rates. If you do have a choice, ask yourself three questions:

- Are you comfortable with your payment amount changing due to fluctuations in interest rates?
- What time-frame are you looking at? The longer the term, the longer you'll need to be ready to accommodate changes to your budget caused by fluctuating rates.
- Where are interest rates now? No one knows whether, when, or how a rate may change. If you choose a variable rate, you're making a bet interest rates will fall.



This chart shows interest earned on a $100 deposit over the course of 40 years at an interest rate of 5%. By the end of the term, $300 (simple) interest has been earned on the principal balance. Over the same term, at the same rate, a $100 deposit would earn $704 compound interest (given a yearly compounding period).

III. "Banking" Your Money

There are three main types of **depository institutions** in the United States: **commercial banks, credit unions**, and **thrifts**. They're all different, and they all offer valuable services.

Commercial banks are like the big box stores of financial services. They offer a little of everything. Commercial banks provide services to both consumers and businesses. They're for-profit businesses, usually run by a board of directors chosen by the bank's shareholders. Consumer accounts at commercial banks carry up to $250,000 deposit insurance coverage provided by the Federal Deposit Insurance Corporation ("FDIC").

Credit unions, which are non-profits, can do just about anything a bank can do. They take deposits, offer loans (both consumer and commercial), and issue credit cards. Credit unions are cooperative, member-owned institutions. The credit union's members elect the credit union's board of directors. Generally, only members may borrow from or deposit money with a credit union. Many credit union accounts carry up to $250,000 deposit insurance coverage per owner, per credit union, from the National Credit Union Administration ("NCUA"). Some may carry private deposit insurance.

Thrifts (**savings and loan associations** and **savings banks**) usually offer services similar to commercial banks. Thrifts may be owned by shareholders, or by their borrowers and depositors. These institutions are called "thrifts," because they originally only offered savings accounts and were limited to mortgage lending. Many are locally-owned and privately managed. Thrift deposit accounts carry up to $250,000 deposit coverage from the FDIC.

Savings Accounts

When you were young, you may have owned a piggy bank. Coin banks like these have been

The United States' Dual Banking System

The United States has a dual banking system. Depository institutions may hold either a national or a state **charter**. National banks with federal charters are supervised by the Office of the Comptroller of the Currency ("OCC") - part of the U.S. Department of the Treasury. Federally chartered credit unions are supervised by the NCUA. State-chartered depository institutions are supervised by state regulators — in Maine, the Maine Bureau of Financial Institutions. Most state-chartered banks also have a federal regulator — either the regional Federal Reserve Bank (*e.g.*, Boston) or the FDIC. National banks aren't subject to state **usury laws**.

around for centuries.[1] Maybe you still use one, or a glass jar, to organize your loose change.

Piggy banks are useful. However, while keeping your money at home may make you feel safe — after all, you'll always know where your money is — it's not necessarily the best idea. You risk losing everything to robbery or fire. You worked hard for your money. Keep it safe.

Savings accounts are safe places to keep your money. The deposited funds are federally insured (see p. 8-9). Depository institutions offer several different types of savings accounts, including:

- **Basic savings accounts**, which offer low interest rates and low minimum deposits, but allow you quick access to your funds in case of emergencies. Credit unions offer similar options, called **share savings** or **primary share** accounts. Federal law limits the number of withdrawals you can make each month;

- **Money market accounts**, which offer slightly higher interest rates and the same protections as basic savings accounts, but require higher minimum balances. Money market accounts allow a limited number of withdrawals each month; and

- **Certificates of deposit ("CDs")**, a/k/a **share certificates** at credit unions, which hold money for a fixed term of a few months to a few years. CDs usually offer relatively high rates. The longer the term, the higher the rate. If you withdraw money from a CD before the end of the term, you may be charged a significant penalty.

Many depository institutions also offer other types of accounts, such as **club accounts** and **individual retirement accounts ("IRAs")**. Take advantage of the savings account options at your bank, credit union, or thrift. Every dollar you save is one less dollar you need to borrow.

Checking Accounts

No matter how you make a living, you need ready access to your money. That's what checking accounts offer. They allow you to access your funds using paper **checks**, **ATM cards**, or **debit cards**. Checking accounts are great for everyday spending; they generally don't have restrictions on how often you can access your money. Just be aware, your depository institution *may* place a limit on the number of daily or monthly ATM withdrawals you can make. Checking accounts come in several varieties:

- **Basic checking accounts** vary from institution to institution, but are the most used type of account. These accounts generally offer little or no interest, but may have perks like online or mobile banking, or "bill pay" services, which let you set up recurring transactions.

[1] Robinson, D. (1924). Some Roman terra-cotta savings-banks. *American Journal of Archaeology*, *28(3),* 239-250. doi:1. Retrieved from http://www.jstor.org/stable/497738 doi:1

- **Joint checking accounts** are checking accounts shared by more than one person. On paper, joint accounts are great. Spouses often use joint accounts to cover shared expenses. If your parents or guardians are listed on your account, they can give you some backup if you run into problems. Be aware: with a joint account no one person controls spending from that account. One partner could overdraw the account, generating fees both would have to cover. Also, all holders on the account can see any transactions. If you're not comfortable with someone else having access to your finances, a joint account is not a good option.

- **Negotiable order of withdrawal ("NOW") accounts** are checking accounts that pay interest on money you've deposited. Some NOW accounts require a significant initial deposit to open. Many have minimum balance requirements. Failure to maintain the minimum balance could result in a penalty fee.

Some checking accounts, especially at large, nationally-chartered institutions, charge monthly maintenance fees when an account holder does not maintain a minimum balance. Other fees associated with checking accounts include **overdraft fees** (see p. 11) and "foreign" ATM fees — charges for using a debit card at an ATM not associated with your institution.

Always use non-erasable ink when writing a check.

Checks

A check is a document telling a depository institution to pay a specific amount of money from an account to a specific person or entity. Checks, also called **negotiable instruments**, have been around for nearly 2,000 years.[2] Modern checks evolved in the 17th century.[3]

Today, checks are printed with the check drawer's (writer's) personal information, the institution's information (including **routing number**), and the check number — all in magnetic ink computers can read.

The first step when writing a check is entering the date. It shouldn't matter what format you use (within reason), as long as the institution can verify the month, day, and year. Next, you need to identify the payee. It's a good idea to ask the payee how this line should read, especially if they have a nickname or are using a business name. After noting the payee, fill in the numerical amount in the **courtesy box** (just to the right of the payee line).

Below the payee line and courtesy box is the **legal line**. Write the dollar amount of the check, in words, on the legal line (*i.e.,* One Hundred Dollars and 00/100 instead of $100.00). If there is extra room after writing the dollar amount, draw a line to the end of the legal line. Make sure the numbers in the courtesy box and on the legal line match. If

[2] Durant, W. (1944). *The story of civilization* (Vol. 3). New York, NY: Simon & Schuster.

[3] Williams, J. (Ed.). (1997). *Money: a history*. New York, NY: St. Martin's Press.

there is a difference between the two, the amount on the legal line will be the amount honored.

Towards the bottom of a check, on the left side, is a memo line. Filling out the memo line is optional, but has benefits. If the check is for a bill, you may want to include the account's number — it'll increase the likelihood of your check being applied to the correct account.

After you've filled in all these lines, review the check. Make sure everything is correct. If you made mistakes, write VOID over the check and start over. If it's a small mistake, like the wrong date or memo, cross it out, write the correct information, and initial next to the correction. Once you're satisfied everything is correct, sign your legal name on the signature line (on the bottom right of the check).

If you write a check and your account doesn't have the funds to cover it, the bank may honor the check, or it may not. In either case, you'll probably be charged a **non-sufficient funds ("NSF") fee**, also called an "overdraft fee," (usually $10-$30) if your account does not have an **overdraft protection line of credit** (see p. 12). If the business tries to deposit that check a second time, you may be assessed a second NSF fee. No matter how closely you watch your account balance, you may, at some point, bounce a check. If you do:

1. Contact the recipient. Let them know you're aware the check bounced.
2. Make good on the check. Pay the outstanding balance. If the business charges a **returned check fee**, pay that as well. Get a receipt.
3. Pay any fees you owe to the bank, and get a receipt.

It's important you correct the situation by depositing funds to cover both the check and any bank fees as soon as possible after bouncing a check. If you don't correct the issue promptly, and if the payee decides to bring a civil action in court, you could end up owing more money, or even attorney's fees.[4]

Debit Cards

Checks have been around for a long time and can be useful, but they're not the only option for accessing money in your accounts. Debit cards are linked to an account at a bank or credit union (usually a checking account). Most depository institutions issue a debit card when someone opens a checking account. Debit cards are flexible and convenient. With each swipe of the card, money is **debited** from the consumer's account to pay for purchases. It can be a challenge to keep track of debit card purchases, since they may take a day or two to clear. Your institution may not immediately post all transactions to your account.

When using your debit card, your transaction may be processed as either a debit, or as credit. If a transaction is processed as credit, a **hold** may be placed on your account. Holds usually

[4] "Civil Liability for Bad Checks," 14 M.R.S. § 6071 (2009).

remain until funds are transferred to the merchant. Hold amounts sometimes exceed the dollar amount of the associated transaction.

Let's say you have $75 available in your account. You go out to eat at a restaurant. The meal costs $30. You pay using your debit card, which is processed as credit. The restaurant may place a hold on your account for $50, to leave room for any additional food ordered or for the tip. Even though your bill was only $30, $50 is "blocked" from your $75 account balance, leaving you with only $25 available. Once the transaction clears and the hold is lifted, all $45 left in your account will be available again.

Overdraft Protection

In general, debit transactions do not go through if there isn't enough money in the account to cover a sale. Some banks and credit unions will process these transactions, charging you a fee if they have signed up for **overdraft protection.**

If you choose to enroll in an overdraft protection plan, your institution may approve ATM, check, or debit card transactions that will overdraw your account. Banks, credit unions, and thrifts generally charge a per-item fee for this service. If your account is

overdrawn, you will receive a notice in the mail about the transaction causing the overdraft. It will tell you the fee, and your current balance. Institutions are required to **charge-off** (close) accounts with negative balances after 60 days. Your institution may charge-off the account after a shorter period of time. (*e.g.*, 30 days). When an account is "charged off" it is no longer active, but you still owe the required balance.

Institutions report charged-off accounts to **ChexSystems** — a **consumer reporting agency**, (see p. 24), which tracks checking and savings account activity. Most depository institutions report information to ChexSystems. If you have a negative balance at your institution, you probably won't be able to open another account somewhere else. You are entitled to one free ChexSystems consumer report each year.

Lost and Stolen Debit Cards

Maine law provides protection against fraudulent debit card charges, but strict time limits apply. If you report a lost debit card or fraudulent charge within two days after you learn of the loss or theft, you may be liable for up to $50. If you notify the bank less than 60 days after you learn of the loss or theft, your maximum liability is $500. If you report a loss or theft more than 60 days after learning about it, you may be liable for all money taken from your account and accounts linked to your account.

Nine Common Sense Tips For Checks and Checking

1. Check your account frequently! Deposit accounts are legal contracts. Make sure you know what your responsibilities are.

2. When you receive a check, always review it as if you wrote it yourself. Have the check's drawer correct any mistakes then and there!

3. Use a **check register** — a booklet used to record checks and other financial transactions — to keep track of your spending. Balance your register periodically to verify how much money you have!

4. You can deposit checks in person, by mail, at some ATMs, at an institution's night drop, or online using a mobile app. When depositing a check, <u>always wait to **endorse** it at the deposit location or teller window</u>. If you lose a check that has already been endorsed, someone other than you could cash it.

5. If you lost a check, or you didn't receive the goods or services you paid for, you can place a written stop payment order on the check (for a fee). A written stop payment is good for six months — the period of time a check is valid from the written date. It stops anyone from receiving funds from that check. If you need to, you can usually renew stop payment orders for another six months (for a fee). Oral stop payment orders last for only 14 days.

6. For some purchases, you may want to consider using a **cashier's check** (also known as a **treasurer's check**). With cashier's checks, the payees usually receive funds faster than they would receive funds from a personal check. If you use a cashier's check, keep it safe. It can be difficult to place a stop on a cashier's check.

7. If a check is made out to two people and the names are adjoined by "and," both parties must sign the check before it's cashed or deposited. If the names are adjoined by "or," only one party on the check needs to sign it.

8. If someone transfers a check to you, some institutions will not honor it unless they can verify <u>both</u> signatures with a photo ID or signature card, the new payee has an account with the institution, and the new payee has matching funds in an account at the institution.

9. Some institutions let you transfer funds in set increments (*e.g.*, $50) from a selected account to cover an overdrawn balance. Your institution may assess a fee for this service.

IV. Investing in Your Future

There are several factors you should consider when building your investment portfolio, including:

- **Your age**. An investment mistake (or loss) late in a person's working career may be almost impossible to correct before retirement. Young people are sometimes willing to accept higher risk in their investments because they have more time to correct mistakes;

- **Your investment goals**. What do you want to accomplish by investing? Do you want to retire in your mid-50s? Early 60s?;

- **Your timeframe**. Some people try to invest so by the time they reach age 40 they can cash in some of those investments and pay off their mortgage. Others plan on investing enough for a comfortable retirement later in life; and

- **Your risk tolerance**. Markets can run in unpredictable cycles. There's no guarantee an investment will rise in value. Most investors want investments that offer high returns with no risk. Investments like that don't exist. The greater the potential return, the greater the risk.

Every investor is unique. Once you've set your investment goals, figure out what investment vehicles are right for you. Many investors favor diverse portfolios: portfolios containing a mix of stocks, bonds, mutual funds, exchange traded funds, bank accounts, real estate, and other investments.

Stocks

Equity securities, also known as **stocks**, represent ownership in a business or venture. There are two main categories of stock. **Common stock** is issued to raise funds, and represents partial ownership in a publically traded corporation. Ownership of common stock generally gives the investor the right to participate in choosing the company's board of directors, and to vote on other matters important to the company. **Preferred stock** is also issued to raise funds. It entitles shareholders to first priority (ahead of common stockholders) when it comes to receiving **dividends** (distributions of a portion of the company's earning) or liquidation of a company's assets.

"Games are won by players who focus on the playing field — not by those whose eyes are glued to the scoreboard."

-Warren Buffett

Historically, stocks perform better than investments in bonds and Treasury bills.[1] In recent years, direct stock ownership of individual common stocks in the U.S. has decreased. As of 2013, only about 13.8% of U.S. households directly held stock.[2]

Bonds

A **bond** is a form of debt. Governments and corporations issue bonds to fund projects or operations, promising to pay investors back, in full, with regular interest payments. Treasury bonds, issued by the federal government, help finance the national debt. Municipal bonds, issued by state and local governments, finance local, public debt. These investments guarantee yields if the bond is held to full maturity. Federal government bonds are considered some of the safest investments, because they are backed by the "full faith and credit" of the U.S. federal government.

Just like other securities, bonds offer some risk. This is especially true of **junk bonds**. Junk bonds offer high returns, but have a much higher default rate than other, investment-grade bonds.

Mutual Funds

Mutual funds are professionally-managed investment funds, which pool money from investors to purchase securities. When investing in mutual funds, you don't get direct stock ownership of common stock. Rather, you're buying shares of a fund run by a professional fund manager. As of 2013, about 8.2% of U.S. households *directly* invested in mutual funds and other pooled investment funds.[3]

Mutual funds can contain a variety of investment products. Some funds are industry specific (*e.g.*, pharmaceutical companies), while others may be based on specific types of

Direct vs. Indirect Investments

Investments can be divided into two broad categories: direct investments and indirect investments. **Direct investments** are investments in **assets** (*i.e.*, things with value). As a result of their investment, the investor owns part of the asset. Investors making **indirect investments** areinvesting in the expertise of people to manage their investment money — buying and selling on their behalf (*e.g.*, investing in a mutual fund or other pooled investment fund). When making indirect investments, the investor does not assume ownership in the assets purchased.

[1] Damodaran, A. (2016). *Annual returns on stock, t.bonds and t,bills: 1928-current* [data file]. Retrieved from http://www.stern.nyu.edu/~adamodar/pc/datasets/histretSP.xls

[2] Bricker, J., Kennickell, A. B., Moore, K. B., Sabelhaus, J. (2012). Changes in U.S. family finances from 2007 to 2010: evidence from the Survey of Consumer Finances. *Federal Reserve Bulletin, 98(2)*. Retrieved from http://www.federalreserve.gov/pubs/bulletin/2012/pdf/scf12.pdf

[3] Board of Governors of the Federal Reserve System (2013). *2013 survey of consumer finances* [data file]. Retrieved from https://www.federalreserve.gov/econresdata/scf/files/scf2013_tables_internal_real.xls

investments (*e.g.,* bonds). Since mutual funds contain many types of investments, investors aren't counting on a particular company's stock performing well to grow their investment. Mutual funds feature **diversification** — reducing investors' exposure to particular assets or risks.

Exchange Traded Funds

Exchange traded funds ("ETFs") are marketable securities that track indices, bonds or commodities. ETFs trade like common stocks. They feature relatively low trading costs and, like mutual funds, can potentially provide the holder with a diverse investment.

Employer-Sponsored Retirement Plans

Employer-sponsored retirement plans fall into two broad categories. **Defined benefit plans** (*e.g.,* pensions) are retirement accounts in which an employer invests funds, and promises employees a set payout upon retirement. Defined benefit plans offer extra security to employees, which comes at the expense of risk to the employer. As such, while defined benefit plans were once common, the number of employees covered by these plans has fallen drastically, from around 60% of workers in 1981 to about 10% in 2003.[4]

As of 2011, **defined contribution plans** were far more common than defined benefit plans.[5] In a defined contribution plan, individual accounts are set up for each employee, and the employer, employee, or both, make contributions to the account. Only contributions to the account are guaranteed, not future benefits. Common plans include:

- **401(k)** accounts: tax-advantaged savings/ investment plans. 401(k) plans allow employees to contribute a portion of their wages to their retirement account.[6] Contributions are deducted from employees' paychecks before tax; as such, tax on 401(k) contributions is usually deferred until retirement; and

"When I was young I thought that money was the most important thing in life; now that I am old I know that it is."

-Oscar Wilde

[4] Buessing, M., & Soto, M. (2006). The state of private pensions: current 5500 data. *Issue in brief, 42*. Chestnut Hill, MA: Center for Retirement Research at Boston College

[5] U.S. Department of Labor (2014). *Private pension plan bulletin: Abstract of 2011 form 5500 annual reports*. Retrieved from https://www.dol.gov/sites/default/files/ebsa/researchers/statistics/retirement-bulletins/2011pensionplanbulletin.pdf

[6] U.S. Department of the Treasury. Internal Revenue Service. (2016, January). Publication 571: Tax-sheltered annuity plans (403(b) plans). Retrieved from https://www.irs.gov/publications/p571/ch01.html

- **403(b)** accounts: similar to 401(k) accounts, but available only to certain types of employees or employees of certain tax-exempt organizations.[7]

Some studies suggest defined benefit plans cost less overall per benefit-level than defined contribution plans.[8]

Brokers and Investment Advisors

It's important to know what you want before making financial decisions. Depending on your goals and timetable, you have many possible options. It's important to know what products you want, and the risk those products present. Investment can be complicated. You may want to consider hiring a broker or investment advisor to help you put together your portfolio. These individuals will manage your investments. Find someone you trust.

When meeting with prospective agents or advisors, always take thorough notes. If an agent or advisor is uncomfortable with you taking notes, they may not be looking out for your best interests. Don't forget to ask questions about compensation. A good agent or advisor will be upfront about how they are paid. If an independent agent or advisor claims they are paid by the company you are investing with, it could end up costing you in fees.

All agents, investment advisors, and their companies operating in Maine must register with the Maine Office of Securities. Make sure your prospective agent or broker is registered. The Office of Securities is a wealth of information about investment. Contact them at (877) 624-8551 if you have questions.

"Just as a cautious businessman avoids investing all his capital in one concern, so wisdom would probably admonish us also not to anticipate all our happiness from one quarter alone."

-Sigmund Freud

[7] U.S. Department of the Treasury. Internal Revenue Service. (2016, August 23). *401(k) plans*. Retrieved from

[8] Almeida, B., & Fornia, W. (2009). Defined benefit plans: A better bang for the buck. *Journal of Pension Benefits, 16(2),* 11-15.

Questions About Taxes?

Even if you don't do your own taxes, you should know at least a little about taxation. Taxes are a complex subject. If you have a question, get in touch with the experts.

The **Maine Revenue Service ("MRS")** is an excellent resource for Maine consumers with questions about taxes. If you need face-to-face help, visit MRS's Maine Taxpayer Service Center. To reach the taxpayer service center, call (207) 626-8475, or visit them at 51 Commerce Dr. in Augusta. Visit MRS online at www.maine.gov/revenue. If you're looking for information on *federal* taxes, the **Internal Revenue Service ("IRS")** is the place to go. Visit the IRS online at www.IRS.gov, or contact them, toll free, at 1-800-829-1040. The IRS has also has three Maine field offices: Bangor (1-207-942-8573), Augusta (1-207-622-1508) and South Portland (1-207-879-4683).

Three Things to Know About Taxes

1. One of three forms is used when filing a federal income tax return: the 1040, the 1040A, or the 1040EZ. The form you use is determined by income level, credits claimed, and the types of income you receive. The 1040EZ is the simplest of the three forms.

2. Most income, including interest earned on deposited money, is taxable. If you earned more than $10 in interest over the course of the year, you should receive a 1099INT form from your depository institution. The 1099INT is an annual tax statement summarizing your interest income for the year.

3. **Tax credits** offset taxes owed. **Deductions** reduce your **taxable income**. Most tax credits reduce your tax liability more than equal-sized deductions, since your income tax is proportional to your taxable income. If you have $10,000 in taxable income at a rate of 10.2% (the U.S. average individual income tax rate in 2016[9]), you might owe $1,020 in income taxes. A $1,000 credit would reduce that amount to $20. A $1,000 deduction would reduce your taxable income to $9,000, resulting in income taxes of $918 — $898 more than with a $1,000 credit. For specific information regarding how credits or deductions may affect your income taxes, contact the IRS or MRS, or consult a tax professional.

[9] Joint Committee on Taxation. (2016, May 10). *Overview of the federal tax system as in effect for 2016*. (JCX-43-16). Retrieved from https://www.jct.gov/publications.html?func=download&id=4912&chk=4912&no_html=1

V. Insuring Your Future

Some risks are easy to avoid; you can avoid the risk of property damage by not owning property. Other risks can be reduced; you can reduce the risk of fire damage by installing working smoke and carbon monoxide detectors. For risks you can't avoid or reduce, you can insure.

Insurance is a type of risk management. It allows businesses or individuals to transfer risk of financial loss from themselves to a third party — an insurance company. In exchange, the insurance company charges a **premium**: monetary compensation. Some insurance companies let policyholders pay their insurance premium in installments; others require policyholders pay the total amount before coverage starts. The amount of an insurance premium depends on a number of factors, including the type of coverage, the likelihood of a claim, and the behavior of the person or business covered by the policy.

An **insurance policy** is a contract between the insurance company and the policy holder; it details the coverage provided by the insurance company. Most insurance policies include a **deductible**: an amount a policyholder must pay out-of-pocket before the insurance company will pay claims.

Claims on insured property are paid using one of two methods specified by the insurance policy: **actual cash value ("ACV")** or **replacement cost**. An ACV policy pays an insured item's replacement cost at the time of loss, less physical **depreciation**. A replacement cost policy pays for the actual cost of replacing the insured item. Insurers often only pay an insured item's actual cash value.

If your insured property is damaged, contact your insurance agent or company right away. <u>Make temporary repairs to protect the property from further damage, but *do not* destroy anything</u>. Photograph or video the damage before making any repairs. Make a list of all damage, and be prepared to explain how it happened. <u>Document all contacts with the insurer and its representatives</u>. Keep track of who said what, and when they said it — including conversations, telephone calls, and e-mail or text chains. A claims adjuster will come to assess and estimate the damage.

The insurer's estimate will include the cost of repairing the damage, the actual cash value, and what the insurer will pay. If you think the insurer's estimate isn't accurate, you may have the extent of the loss appraised. If you do, you and the insurer will each hire an appraiser. If the appraisers cannot agree on the amount of the loss, they will select someone to make the final decision.

Auto Insurance

Auto insurance policies insure against damage to vehicles and associated expenses. People usually purchase auto insurance for terms of six months to one year. Policy premiums can vary widely; comparing premium quotes before purchasing is a good idea. There are several types of auto insurance available to motorists:

- **Bodily injury liability coverage** insures against injury to people, not damage to vehicles. It covers claims against you if you injure or kill someone while driving. Depending on your policy, bodily injury liability coverage may also cover family members driving an insured vehicle.

- **Property damage liability coverage** protects you if you damage some else's property with your vehicle.

- **Uninsured motorist coverage** protects you against the cost of injuries sustained in an accident caused by a driver without required insurance, or who cannot be identified.

- **Underinsured motorist coverage** is similar to uninsured motorist coverage, but insures against drivers with insufficient coverage, rather than drivers without coverage.

- **Medical payment coverage** pays for medical and funeral expenses you (or others riding with you) incur if you (or they) are hurt or killed in an accident, even if you are at fault. It also covers both you and family members in your household for injuries caused by another vehicle while walking or biking, or riding in another car.

- **Collision coverage** pays for physical damage to your car if it collides with another object (*e.g.,* a tree). Collision coverage is optional unless contractually required. If you have an older car, you may

If You Are in an Accident...

- Call the police, and ask for a copy of the accident report after they complete it.

- Request the other driver's information (contact information, insurance information, and license plate numbers). If possible, try to validate it.

- Take pictures of the damage as evidence for proof of fault, and write down details of the accident while they are still fresh in your mind.

- Immediately file a claim with your insurance agency. They will conduct an investigation based on the report, and may contact any witnesses at the scene. The insurance company will tell you the status of your claim following the investigation.

not want to buy collision coverage. It can be relatively expensive compared to the vehicle's actual cash value.

- **Comprehensive coverage** pays for damage to vehicles from most causes other than collision, such as fire, flood, or theft. Comprehensive coverage also covers broken glass (*e.g.,* windshield damage). Like collision coverage, comprehensive coverage is optional unless contractually required.

Many states require that drivers purchase minimum liability coverage for their vehicle. Maine currently requires drivers to carry liability, uninsured motorist, and medical payment coverage.

In Maine, insurance companies may cancel policies for any reason during the first 60 days after the policy is signed. After 60 days, the insurer may cancel the policy only for reasons allowed under the **Automobile Insurance Cancellation Control Act**. These reasons include nonpayment of premium, fraud or misrepresentation affecting the policy, violation of terms and conditions, and license suspension or revocation, among others.

Health Insurance

Health insurance covers the cost of medical expenses. It helps ensure you can afford necessary medical care. Premium rates vary based on the type of plan, cost-sharing and benefits. Other factors, such as your geographic area, whether you smoke, and your age, may also affect your premium rate. Like auto insurance, health insurance comes in many different varieties.

Private health insurance is coverage individuals can purchase from private companies. You can purchase private health insurance individually, through a group (*e.g.*, your employer), or through an Individual Marketplace established by the Affordable Care Act. There are several types of private health insurance coverage.

In **fee-for-service plans,** an insurance company reimburses the policyholder for part of or all healthcare expenses incurred. Fee-for-service plans allow individuals to choose their own primary care providers ("PCPs").

Managed health care plans require policyholders to receive health care services through a network of hospitals and other medical providers ("**preferred providers**"). Preferred providers agree to charge reduced fees. As such, they tend to be both cheaper and more restrictive than fee-for-service plans. Managed healthcare plans generally fall into two categories:

- **Health maintenance organizations ("HMOs")** contract with select health care providers. With an HMO plan, you must choose a primary care provider from the plan's participating providers. For non-emergency hospital or specialty care, you must get a referral from your primary care provider. Out-of-network providers are not usually covered under HMO plans, unless no in-network provider can provide the services needed.

- **Preferred provider organizations ("PPOs")** combine aspects of both fee for service plans and HMOs. As with an HMO, you must choose a PCP from a list of participating providers. For non-emergency hospital or specialty care, you must get a referral from your PCP first. You may see out-of-network providers, but you will pay more than you would to see an in-network provider. Out-of-state providers may or may not be covered.

If you use an out-of-network provider, your share of the costs (*e.g.,* co-pays, deductibles, etc.) will be higher. Most plans include an **out-of-pocket limit**: the maximum amount you will ever have to pay out of your own pocket for health care in a given year. If you use an out-of-network provider, you may have separate in-network and out-of-network out-of -pocket limits, which can add significant expense.

Homeowners Insurance

Homeowners insurance protects your home against theft and other losses. It also protects against liability claims for accidents that may happen on your property. Homeowners insurance premiums are often paid yearly. Your policy should cover your loan balance, the value of your assets, and the amount needed to replace your property should it be destroyed. That figure isn't necessarily the same as the minimum required by your insurance company. If you live in an area at high risk area for certain events (*e.g.,* floods), consider purchasing additional coverage.

Life Insurance

Life insurance pays a beneficiary when a policyholder dies. Not everyone needs life insurance. However, it's a wise choice for some. Life insurance payments may cover burial and funeral costs, help maintain financial support for the policyholder's family, or pay

When buying insurance...

- Know what insurance coverage is required by law and what you may be required to have by contract. Does your landlord require renters insurance? Does your auto financer require collision insurance?
- Find a knowledgeable broker or agent who can explain the product. Ask for a referral from someone in your network, or visit enroll207.com/locator to find Maine brokers and agents.
- Make sure you understand the product you're buying. Always ask questions! What's covered under the policy and what isn't? Are there any deductibles or co-pays?
- Get a copy of your insurance contract and read it! If you have any questions, call the Maine Bureau of Insurance at 1-800-300-5000.

off debts the policyholder left behind. If you decide to purchase life insurance, make sure you do so through a well-established, financially-sound company. There are several different types of life insurance.

- **Term life insurance** is restricted to a set time period. Once the period is up, the insurance company will not pay benefits if the policyholder dies.

- Unlike term life insurance, **whole life insurance** provides coverage regardless of how long the policyholder lives, so long as he or she continues to pay premiums. Whole life insurance also acts as an investment. Part of each payment covers the premium, and part is invested by the insurance company on behalf of the policyholder.

- **Universal life insurance** provides coverage for a specified term, but also incorporates a savings element. This type of insurance allows policyholders to temporarily raise their insurance benefits via a **term rider**.

Annuities

Annuities are contracts guaranteeing payments at a future point — usually retirement. Annuities are complex, but can be powerful investment tools. The value of your investment at the completion of the contract depends on the type of annuity.

- **Fixed annuities** feature payouts in regular installments.

- **Variable annuities** feature payouts based on a guaranteed number of units, with unit values and payments depending on the value of underlying investments.

- **Equity indexed annuities** guarantee a minimum interest rate. However, the actual performance of the account is determined using a market index, such as the S&P 500.

Annuities are generally not very liquid, meaning the money is not easily accessible. An early withdrawal from an annuity can result in a penalty. It's a good idea to treat annuities as long-term investments.

Need Help?

The Maine Bureau of Insurance (1-800-300-5000 | www.maine.gov/pfr/insurance) is a wealth of information on insurance matters. Staff can answer questions about insurance options, policy contracts, and the individual marketplace. The Bureau of Insurance can also assist with the insurance claims process and help resolve complaints against insurance companies.

VI. Understanding Credit

Debt and credit are part of the same transaction. Credit is borrowed money. It's as close as your local bank, or a click of your mouse. It can be a useful tool when handled responsibly. Credit lets you make a purchase today, and repay it over time. Imagine having to save for 20 or 30 years just to buy a home!

Credit Reports

A credit report is like school transcript. It's a snapshot showing how someone has performed on financial obligations. Credit reports consist of **tradelines**: records of individual accounts. Each tradeline shows the name of the lender, the type of loan, how much was borrowed, monthly payment amounts, whether payments were made on time, and the loan's current balance. Legal actions, like tax liens, may also appear on a credit report.

Lenders like to see **positive tradelines** — tradelines showing consistent on-time repayment of debt — on credit reports. Credit reports can also include **negative tradelines**: tradelines that may make it difficult get a loan, find a job, or rent an apartment. Common negative tradelines include repossessions, foreclosures, and bankruptcies. Most tradelines, positive or negative, remain on a person's credit report for up to 7 years. Some, including Chapter 7 bankruptcies, may remain on a credit report for ten years or longer.

Credit reports are compiled by **consumer reporting agencies ("credit bureaus"):** companies that collect consumer information and make it available to other businesses. Most credit reports are compiled by the "big three" credit bureaus: Equifax, Experian, and TransUnion. All three operate nationwide. If you grew up in Maine and decide to move to Florida, your credit history — good or bad — will follow you south.

The Fair Credit Reporting Act's ("FCRA's") FACT Act allows consumers one free credit report from each of the big three credit bureaus each year. The Bureau recommends obtaining a copy of your credit report from one of the big three credit bureaus every four months. To get a copy of your credit report, for free, visit www.AnnualCreditReport.com or call, toll free, 1-877-322-8228. You can also use the form found on page 43 of this booklet.

When you contact the credit bureau, they will ask you to provide personal identification information (*e.g.,* name and Social Security number) to confirm your identity. If you requested a credit report online, it should be provided immediately. If you called to request your credit report, it should arrive in the mail within a few weeks. Once you receive your report, review it for accuracy. Instructions on how to challenge incorrect or missing items should be provided with the report.

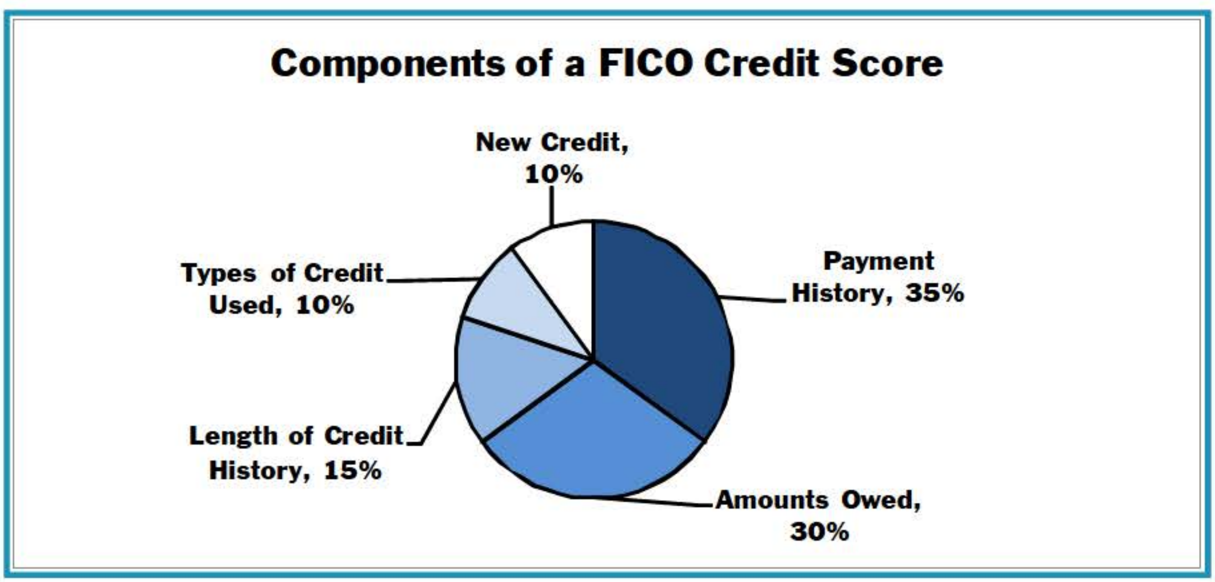
Credit Scores

A **credit score** is a numerical representation of a person's creditworthiness, calculated using information from his or her credit report. Your credit score is an important tool for understanding your finances. A high score enhances your ability to borrow at the best rates and terms available. Unlike credit reports, which you can get for free once each year, credit bureaus will charge you a fee to access your credit score.

The most widespread credit scoring model in the U.S. was developed by Fair Isaac Corporation ("FICO"). FICO scores range from a high of 850 to a low of 300. The higher people's credit scores, the greater their presumed creditworthiness. FICO's model takes several factors into consideration. Each factor is weighted differently for different groups of people (*e.g.,* an established homeowner vs. a recent high school graduate). For most people:

- 35% of their FICO score represents payment history.
- 30% represents amounts owed.
- 15% represents length of credit history.
- 10% represents new credit.
- 10% represents the types of credit used.

People who pay their loans on time, keep their credit card balances low, and don't overextend themselves financially often have relatively high credit scores in the mid 700s to low 800s. On the opposite end of the spectrum are borrowers who don't honor obligations and have histories of late payments. This can result in low credit scores (below 600). Borrowers with low credit scores are more frequently turned down for loan requests, and, even if approved, pay higher APRs than borrowers with excellent credit histories.



Credit scores are a reliable way for lenders to determine the risk of borrowers defaulting or becoming delinquent. The lower the credit score, the higher the risk to the lender (and the higher the interest rate charged). Students entering the workforce often begin adulthood with relatively low credit scores. Over time, the addition of positive trade lines raises their scores, allowing easier access to financing.

Building Credit

When you're just starting out, establishing credit can be frustrating. You may lack the credit history to get the loan you want. Although it may seem like a challenge, building credit is a straightforward, structured process. Again, everyone's situation is different. Here are a few common sense suggestions to help you build credit if you're just starting out:

- Look into a **passbook loan**: a personal loan extended by a depository institution to a savings account holder. The borrower's savings account balance serves as collateral on the loan; the amount of the loan cannot exceed the borrower's savings account balance. The lending institution may place a hold on the funds in the savings account until the loan is fully paid off.

- If you're looking at buying a vehicle, save up a large **down payment** (20% or more). Lenders are more apt to approve an auto loan request with a large down payment, because less money is financed, meaning less risk.

- Find a **cosigner**: someone to guarantee repayment of the loan. Many people's first credit experience is with an adult cosigner assisting them on their first loan. Cosigners must be 18 years or older, and should have a better than average credit history. Asking someone to cosign a loan is a serious commitment. Cosigners are 100% liable for repayment on a loan.

- Consider applying for a credit card with a low **credit limit** (*e.g.,* $1,000). Make sure

Types of Credit

There are two main types of credit. **Installment credit** is a type of credit where a creditor loans a specific amount of money, which the borrower agrees to repay in a fixed number of payments over a specific period of time until the account balance amortizes to $0. Credit where borrowers are given access to a **line of credit**, which they can draw on to make purchases, is called **revolving credit**. As money is repaid, it is automatically available to be borrowed again.

Either installment credit or revolving credit may be secured or unsecured. With **secured credit**, the borrower pledges an asset as **collateral**. If the borrower defaults, the creditor may take possession of the pledged asset. **Unsecured credit** is credit where the borrower is not required to pledge collateral. Unsecured loans, including most credit cards, are risky for lenders. As such, they tend to feature higher APRs than secured, collateralized loans.

you pay that card's balance in full each month.

Once you've established a credit history, *maintain* it!

- Make all your payments on or before the due date — not just with credit; with all household bills, too. Long-term unpaid bills, such as utilities, will negatively affect your credit report.
- Your **credit utilization ratio** matters. Keep your balances low on revolving accounts, such as credit cards. Using a high percentage of your credit, even if you pay it monthly, can negatively affect your credit score. If you have a credit card, keep your balance at less than 30% of your credit limit.
- Watch how many accounts you open. More credit isn't necessarily a good thing. Creditors take into account how much credit is available to you. Having too much potential debt available through multiple credit cards or other revolving loans will negatively affect your credit score.

File Freezes

File freezes lock down your credit report, preventing credit bureaus from releasing your information to third parties without your authorization. Placing a file freeze on your credit file does not freeze your credit cards, debit cards, or existing loans. Your insurance providers, who check your credit reports periodically, also retain full access to your credit report during a file freeze.

Maine has one of the strongest file freeze laws in the nation. Take advantage of it! By calling each of the numbers at the bottom of this page, you can lock down your credit reports, preventing thieves from applying for loans, housing, or benefits in your name. If you place a file freeze online or by phone, be prepared to provide personal information. The credit reporting agency will need it to confirm your identity. When writing, ask the agency to freeze your file under Maine's file freeze law. Make sure to provide the credit reporting agency with your Social Security number, your date of birth, and your mailing and street addresses. Don't forget to sign the letter!

The credit reporting agency will mail you a personal identification number ("PIN"), and

To place your free file freeze, contact:

Equifax	**Experian**	**TransUnion**
PO Box 105069	PO Box 4500	PO Box 2000
Atlanta, GA 30348	Allen, TX 75013	Chester, PA 19016
1-800-349-9960	1-888-397-3742	1-888-909-8872
www.freeze.equifax.com	www.experian.com/freeze	www.transunion.com/freeze

will provide instructions for lifting the security freeze. Don't lose your PIN - you will need it to remove the file freeze. Your file freeze will remain active until you tell the credit reporting agency to lift it. Under Maine law, there is no fee for freezing or unfreezing your credit file. However, credit reporting agencies may charge "protected consumers" (people under the age of 16) a nominal fee of $10 or less to place or remove a security freeze.

Auto Loans

An auto loan is a loan taken out to purchase a vehicle. Auto loans are a type of installment credit, usually secured by the vehicle the borrower purchases. Before buying a vehicle, check your finances. Ask yourself a few questions:

- Can I afford to pay cash?
- If I borrow, can I afford the monthly payments, given a reasonable repayment period?
- What impact will this purchase have on my lifestyle and budget?

When looking for a vehicle, research what makes and models meet your needs. Check online to figure out a fair price, and a fair price for your trade-in (if you have one). Private websites, including KBB.com, NADA.com, and Edmunds.com, can help you determine fair selling prices for both new and used automobiles.

For more information about financing the purchase of an automobile, see the *Downeaster Common Sense Guide to Automobile Buying and Financing*. See p. 41 for ordering details.

If you can't afford to pay cash, contact local banks and credit unions to get quotes for both APRs and loan terms. Make sure potential lenders don't check your credit report when you call to get a quote; multiple **hard pulls** on your credit report may lower your credit score. Don't go to the dealership without figuring out who offers the best deal. Shop for APRs first!

Be professional! Let the dealership know you're coming. Call to make an appointment, preferably about a week before the end of the month (when you may be able to get a better deal). Don't be afraid to negotiate. Establish your price floor and work up from there. Never feel you need to buy *this* vehicle. There are always other options. Be firm, but realize the dealership is a business and needs to make a profit.

After negotiating a sale price, it's time to close the deal. Finance through the dealership only it offers better terms than other lenders you're spoken with. The dealer may offer to finance the vehicle with no money down. It may sound like a good option, but no money down financing could cost you more in the long run. Consider making a down payment of 10-15% of the purchase price. The dealer may suggest add-ons, such as an extended warranty plan. Whether you purchase any of these products is up to you; make sure any additional products you purchase make good financial sense for your situation. Above all else, make sure you read everything before you sign.

Credit Cards

A credit card is a small plastic card issued by a bank, credit union, or other lender, which provides the **cardholder** access to a revolving loan. Credit cards are relatively easy to obtain, even for the financially challenged. Credit cards are not extra cash. They are unsecured loans, which must be paid back.

Card issuers used to be very active on college campuses, marketing credit cards to students with little or no income. The Credit Card Accountability, Responsibility and Disclosure Act of 2009 ("CARD Act") put an end to these practices. Responsible credit card users:

- Pay their balances in full every month, avoiding finance charges;
- Choose credit cards with low APRs and low or no annual fees;
- Generally restrict credit card usage to travel and emergencies, and occasional in-person or online purchases; and
- Carry no more than three credit cards.

When using a credit card, you're drawing on a line of credit provided by the card issuer, and are responsible for repaying the amount borrowed — with interest. Credit cards offer financial protections under the Truth-in-Lending Act, limiting your liability for unauthorized transactions to no more than $50 per card/account.

Credit cards feature minimum monthly payments — usually about 4% of the card's balance. If a cardholder's current balance is $5,000, the minimum monthly payment will likely be around $200. Most credit cards feature extremely high APRs — sometimes four to five times higher than those on mortgage or car loans. This is, in part, because credit cards are risky for lenders. Unlike mortgages or car loans, credit cards generally don't feature collateral pledged as security.

According to the U.S. Census Bureau, in the second quarter of 2016, online sales comprised roughly 8.1% of retail sales in 2015.[1] With so much shopping happening online, it's especially important you take precautions to protect your money.

- Enter credit card details only on secure sites. If the web address begins with "https," the site uses encryption to transmit data, making it more secure.
- Buy only from legitimate, trusted retailers. If you can't find any impartial reviews on a website, be cautious about purchasing anything from it.
- Don't save your credit card information in your browser or in website payment portals. If you don't want to give up the

For more information on credit cards, see the *Downeaster Common Sense Guide to Credit Cards — Paper or Plastic?*. See p. 41 for ordering details.

[1] DeNale, R., & Weidenhamer, D. (2016, August 16). Quarterly Retail E-Commerce Sales. *U.S. Census Bureau News.* Retrieved from http://www.census.gov/retail/mrts/www/data/pdf/ec_current.pdf

convenience of one-click shopping, create a strong password (at least 10 characters, featuring upper & lowercase letters, numbers, and symbols) for each site. Use unique passwords for each site you visit. If one is compromised, it won't affect the others.

Student Loans

Knowledge is often the gateway to a successful future. However, earning a college degree can be expensive. Student loans are big business. As of 2016, American students (and their cosigners) owed more than $1 trillion in student loans[2]. Student loans may be backed by the federal government or issued by a private company. Repayment terms on federally-backed student loans are generally more favorable than those of private student loans.[3] Approach borrowing for college as a savvy consumer, using the same comparison shopping skills you would for any other loan.

Before you finance your education, comparison shop for schools offering programs that interest you. Consider in-state options. If you plan on teaching, the difference in cost between a four-year degree at an in-state institution, like the University of Maine at Farmington, and a private college outside of Maine can be significant. Choosing an in-state college sometimes makes more financial sense when it comes to repaying an educational loan. If you choose to complete your undergraduate degree through the University of Maine system, you will likely spend less than $40,000.[4] A similar degree at an out-of-state public institution could cost more than twice as much.[5] Remember: you must pay back all student loans you take out. Student loans are rarely forgiven, even in bankruptcy. Make sure the cost of the school you choose is reasonable given your financial situation and potential earnings in your field of study.

[2] Board of the Governors of the Federal Reserve System. (2016). *Consumer credit August 2016: Federal Reserve statistical release G.19.* Retrieved from http://www.federalreserve.gov/releases/g19/current/g19.pdf

[3] U.S. Department of Education Office of Federal Student Aid. (2016, Nov. 2). *Federal versus private loans.* Retrieved from https://studentaid.ed.gov/sa/types/loans/federal-vs-private

[4] College Board. (2016). *Average 2016-17 In-state and out-of-state tuition and fees at public four-year institutions by state and five-year percentage change in inflation-adjusted in-state tuition and fees* [data set]. Retrieved from https://trends.collegeboard.org/sites/default/files/cp-2016-figure-7.xlsx

[5] Ibid.

The Finance Authority of Maine's ("FAME's") Higher Education Division is an excellent go-to source for Mainers with student loan questions. If you have questions about financial aid, call FAME's hotline at 1-800-228-3734. In addition to providing resources such as loan comparisons and calculators, FAME administers "The Loan for ME" program. This program features fixed rate private student loan options for Maine consumers. You can find out more about The Loan for ME at www.theLoanforME.com.

Personal Loans

Personal loans are small, unsecured loans — often in the $1,000-$5,000 range. Consumers use personal loans to bridge short-term financial needs. Personal loans are expensive. Like credit cards, they are unsecured, and offer high risk to the lender. As such, personal loans often feature APRs of 18% or higher, making them among the highest-cost types of credit available. For more information about personal loans, check out the *Downeaster Common Sense Guide to High Interest High Cost Loans*, available free from the Bureau of Consumer Credit Protection. See p. 41 for ordering details.

Payday Loans

Payday loans are short-term, high-cost loans. In Maine, payday lenders must hold a license with the Maine Bureau of Consumer Credit Protection. Under Maine law, fees on payday loans of $250 or more are limited to $25. Illegal lenders, especially those found online on the Internet, have little concern for following laws. Unlicensed payday lenders frequently offer loans with APRs in excess of 400%. The APRs on illegal payday loans are high enough that even on small loans of $300-$500, it may be impossible to pay off the principal balance. For more information on payday loans, check out the *Downeaster Common Sense Guide to High Interest High Cost Loans*, available free from the Bureau of Consumer Credit Protection. See p. 41 for ordering details.

X. Debt Collection

There's no such thing as a free lunch. If you fail to repay a financial obligation, a debt collector may contact you! Debt collectors are subject to restrictions under the federal **Fair Debt Collection Practices Act**, and certain state laws, including the Maine Fair Debt Collection Practices Act. Debt collectors must:

- Call only between the hours of 8AM and 9PM;

- Validate a debt if the consumer requests, in writing, they do so;

- Not contact third parties (*e.g.,* a consumer's family members or co-workers) regarding a debt, other than to confirm the debtor's location; and

- Not harass borrowers by using threatening or obscene language, or cause the consumer's phone to ring repeatedly or continuously with the intent to harass or annoy.

Legitimate debt collectors can't use false or misleading statements to collect debts. However, some illegal, unlicensed collectors don't play by the rules. They may threaten you with arrest, imprisonment, or wage garnishment without a court order. They may (or may threaten to) call neighbors, friends, family, or coworkers to coerce their target into wiring money. They may even threaten to foreclose on your home.

In Maine, debt collectors, other than attorneys admitted to the Maine Bar, must hold a license with the Maine Bureau of Consumer Credit Protection. If you've been contacted by a debt collector and have questions or aren't sure the collection agency is licensed, contact the Bureau at 1-800-332-8529.

"Credit is a system whereby a person who can not pay gets another person who can not pay to guarantee that he can pay."

-Charles Dickens

Working With Collectors

If you communicate with a debt collector, be cautious. Make sure they are licensed, and make sure the debt is valid before you send money. <u>Don't admit responsibility for a debt until you are sure the debt is yours</u>. Ask for written validation within 30 days of the collector's first communication with you.

Be polite and honest when working with the collection agent. If the collector wants to communicate by telephone, tell him or her the best times to call. If telephone contact isn't convenient for you, ask them to send all communications by mail. Keep the lines of communication open. Reply promptly if a collector sends a letter or leaves a message, even if you can't make your payment.

If you are not able to pay the debt all at once, try to establish a repayment plan with the debt collector. The collector may or may not agree to a repayment plan. Make sure your offer is reasonable. If you owe $5,000 and offer to pay $5 each month, it would take *83 years* to repay the debt! An offer of $250 each month would repay the debt in 20 months. If you are on a fixed income or are not able to pay back the debt, provide proof to the collector. They may be more willing to work with you to find suitable repayment options. If you negotiate a payment plan or settlement offer, the collection agency must provide you a written copy of the agreement within 10 days of entering into it.

<u>Make only promises you can keep</u>. If you've established a payment plan, make sure you can afford the periodic payment amount you've agreed to. Failure to honor a repayment plan may result in the debt collector or creditor taking you to court.

XI. Avoiding Scams

Just because someone advertises an item or service for sale at a "too-good-to-be-true" price doesn't necessarily mean the offer is legitimate. It may be a scammer trying to make money at your expense. Luckily, most scams share some common characteristics:

- **Unsolicited Contact:** If you receive a phone call, e-mail, fax or advertisement from a person or company you're not familiar with, be wary. Many scammers use unsolicited messages to find victims.

- **Incomprehensible Investments:** Before agreeing to anything, make sure you understand what's being offered. Scammers use confusion to make themselves sound like experts. <u>Ask questions and, if you need to, ask for help from someone you trust</u>.

- **"Act Now!":** Scammers want you to act fast, before you have a chance to think or ask others for advice. <u>Don't be pressured into making a quick decision.</u>

- **Suspicious Payment Methods:** Many scammers ask people to send money via unstoppable or difficult-to-trace methods (*e.g.,* wire transfer or gift cards). Before sending money to a person or business you aren't familiar with, ask yourself "Why won't they let me use a different payment method?"

- **Paying Money to Get Money:** Many scammers ask victims to pay fees for "administrative costs" or "taxes" in exchange for a much larger sum of money. <u>Never pay money to get money</u> – it's a hallmark of financial scams.

- **The Deal of a Lifetime:** Watch out for promises of high returns with little or no risk. <u>There's no such thing as a free lunch. Without risk, there is no reward</u>.

- **"Trust Me":** Scammers often ask potential victims to wire money or reveal personal information based on trust. Ask yourself, "Do I really know who this is? Why should I trust an unsolicited offer from a stranger?"

- **"Tell No One":** Many victims report being instructed to keep a potential "deal" secret. Trust your family and friends. The more people you tell the pitch to, the better the chance someone will be able to determine whether it's a scam. Always ask yourself "Why would a stranger pitch this deal to me?"

Take a deep breath, pause, and ask questions. <u>Don't act impulsively</u>! <u>Guard your personal information</u> (date of birth, street or mailing addresses, Social Security number and bank account numbers) – especially during initial calls. Ask for the caller's full name, email address, the legal name of the company (as registered with the Maine Secretary of State's Corporation Division), the company's physical and mailing addresses, and their State of Maine license or registration number. If they refuse, don't do business with them! If they comply, call the appropriate government agency (see pg. 44) to determine if the business and sales pitch are legitimate.

The *Downeaster Common Sense Guide: Gone Phishing — Identifying and Avoiding Consumer Scams* contains more information about common scams and how to avoid them. Maine residents can receive a free copy by calling 1-800-332-8529, or by viewing online at www.Credit.Maine.gov.

A Few Common Scams

- **IRS scammers** claim they are Internal Revenue Service agents who need immediate access to a consumer's bank account(s) due to fraud or tax issues. The rattled consumers give the information to the "agent," who debits money from victim's account. As of 2015, IRS impersonation scams were the most common type of scam reported to the U.S. Senate Aging Committee's Fraud hotline[1].

- In **tech support scams**, a consumer receives a call from someone claiming they have detected a virus, malware, or other issue with the consumer's computer. After gaining the consumer's trust, the caller may have them perform a series of tasks to find the "problem." Once the consumer is convinced there is a serious issue, the caller asks for personal information, gains remote access to the computer, or tricks the consumer into installing harmful software.

- In **utility billing scams**, a consumer receives a call from someone claiming to represent a utility, and is warned they're behind on payments. The caller claims if the victim doesn't pay immediately (sometimes an amount several times the consumer's monthly bill), the victim's service will be terminated. Although utility scammers sometimes ask for credit card information, they're more likely to ask for prepaid cards, money orders or wire transfers.

- In **lottery scams**, a consumer receives an unexpected call, e-mail or letter informing them they have won a large sum of money in a foreign lottery. The scammer asks the victim to send money for "processing fees" or other charges before they release the winnings. It's not possible to win a lottery without purchasing a ticket. If you haven't purchased a ticket, you can't have won!

[1] U.S. Senate Special Committee on Aging. (2016). *Fighting fraud: U.S. Senate Aging Committee identifies top 10 scams targeting our nation's seniors*. Retrieved from https://www.aging.senate.gov/imo/media/doc/217925%20Fraud%20Book%20Final.pdf

Glossary of Terms

401(k): A type of retirement plan that allows employees to invest salary deferral contributions. *See* ***Defined Contribution Plan.***

403(b): A type of retirement plan offered by non-profit and public institutions and organizations. Similar to 401 (k) plans, 403(b) plans allow employees to invest a portion of their income, tax-deferred. *See* ***Defined Contribution Plan***.

Actual Cash Value ("ACV"): A method of establishing the value of insured property. Often calculated as the cost to repair or replace damaged property or the property's fair market value.

Amortization: The gradual paying-down of debt by installment payments.

Annual Percentage Rate ("APR"): The total cost of consumer credit expressed as a yearly rate.

Annual Percentage Yield ("APY"): The total rate of compounded interest for a one year period.

Annuity: A contract sold by life insurance companies guaranteeing a fixed or variable payment at some future point.

ATM Card: A card issued by a financial institution with allows the cardholder to perform transactions at an automated teller machine ("ATM").

Available Balance: The portion of an account balance available to spend. Available balance often differs from the actual account balance.

Bank Check: *See* ***Cashier's Check***.

Bond: An interest-bearing security obligating the issuer to pay the bond holder a specified sum of money, usually at regular intervals.

Borrower: A person who receives a loan.

Cardholder: A person who holds a credit, debit, or other card issued by a financial institution.

Cashier's Check: A check written by a financial institution on its own funds.

Certificate of Deposit ("CD"): A savings certificate issued by a financial institution, usually with a fixed maturity date and interest rate. CDs generally restrict access to the funds deposited until the investment's maturity date.

Charter: a document outlining the conditions under which a financial institution or other body is organized, and defining its rights and privileges.

Check Register: A journal used to record checks and payments.

Check: A written order directing a back to disburse money to a named person or entity.

Checking Account: An account against which checks can be drawn.

Closed-End Credit: Credit in which proceeds are disbursed in full when the loan closes, to be repaid by a specific date.

Club Account: A type of interest-bearing savings account, generally set up to save for a specific purpose.

Collateral: Something pledged as security for the repayment of a loan, to be forfeited in the event of default.

Collision Coverage: A type of automobile insurance that reimburses the insured for damage sustained to their automobile.

Commercial Bank: A type of bank that provides loans and other products, such as CDs and checking accounts.

Common Stock: A type of security representing ownership in a corporation.

Compound Interest: Interest earned on principal plus interest earned earlier.

Comprehensive Coverage: A type of automobile insurance that insures vehicles against damage from causes other than collision.

Consumer: A buyer of a good or service.

Cosigner: A third party to an obligation, who guarantees the obligation will be repaid.

Credit Bureau: *See* ***Credit Reporting Agency***.

Credit Card Accountability Responsibility and Disclosure Act ("CARD Act"): A federal statute aiming "...to establish fair and transparent practices relating to the extension of credit under an open end consumer credit plan, and for other purposes."

Credit Card: A type of purchase device that accesses a revolving loan for consumer purchases. It allows consumers to charge purchases today and pay for them later, with added interest.

Credit Limit: The highest balance allowed by a creditor on a credit account. Typically associated with a credit card or home equity line of credit.

Credit Report: A detailed record of a consumer's credit history prepared by a consumer reporting agency. Credit reports are used by lenders as a means of determining a potential borrower's creditworthiness.

Credit Reporting Agency: Any person or company that engages in the practice of assembling or evaluating consumer credit information or other information on consumers for the purpose of furnishing consumer information to third parties.

Credit Score: A statistically-derived representation of a consumer's creditworthiness expressed as a number.

Credit Union: A member-owned financial co-operative, operate by its members and that share profits amongst its owners.

Credit Utilization Ratio: A measure of how much a borrower owes compared to the amount of credit available to that borrower. Calculated as the total debt balance of a borrower, divided by the total (used and unused) amount of credit available to a borrower.

Critical Thinking: Objective analysis and evaluation of an issue to form a judgment.

Custodian: An entity responsible for keeping and safeguarding funds.

Debit: in banking, removing money from a customer's account, typically as payment for goods or services.

Debit Card: A type of payment method that uses a consumer's funds (usually from a checking account) to make a purchase.

Deductible: In insurance, an out-of-pocket amount the insured must pay before an insurance company pays a claim.

Deduction: In taxation, reduction in tax obligation from a taxpayer's gross income.

Default: Failure to fulfill an obligation (*e.g.*, repay a debt).

Deficiency Balance: The remaining amount due after collateral securing a loan is sold for less than the outstanding balance of that loan.

Defined Benefit Plan: A type of retirement plan in which an employee's pension payments are calculated according to length of service and the salary that employee earned at the time of retirement.

Defined Contribution Plan: A type of retirement plan in which a company sets aside a certain amount or percentage of money for the benefit of each of its employees.

Delinquency: Failure to make a payment on an obligation when due.

Depository Institution: A type of financial institution that accepts monetary deposits from consumers.

Depreciation: A reduction in the value of an asset over time, often due, at least in part, to wear and tear.

Direct Investment: The purchase or acquisition of a controlling interest in a business by means other than outright purchase of shares.

Disbursement: Loan proceeds paid to a borrower.

Diversification: The act of spreading out risks in an investment portfolio.

Dividend: A distribution of earnings to shareholders.

Down Payment: An amount or percentage of the sales price that a consumer pays up-front before financing the balance of the sales price. Down payments made by a borrower lower risk to the lender.

Endorsement: A signature acknowledging both parties agree to the exchange of funds on a check.

Equity Indexed Annuity: An annuity in which yield is partially based on an equities index. *See* ***Annuity***.

Escrow Account: An account established by a lender to ensure real estate tax and insurance billings are paid in a timely manner. Escrow accounts are mandatory for loans with high loan-to-value ratios, and may be established by lenders at any point by virtue of the mortgage agreement.

Fair and Accurate Credit Transactions Act ("FACT Act"): Federal law amending the Fair Credit Report Act, and allowing consumer to request and obtain a free credit report once every year from each of the three major credit reporting agencies.

Fair Credit Reporting Act ("FCRA"): Federal law that regulates the collection of credit information.

Fair Debt Collection Practices Act ("FDCPA"): Federal law which regulates the behavior of third-party debt collection businesses.

Fair Isaac Corporation ("FICO"): A publicly traded analytical firm hired by credit reporting agencies and lenders to gauge the credit risk of loan applicants. FICO uses a highly advanced proprietary algorithm to assign a credit score that ranges between 300 and 850 points.

Fee For Service Plan: A payment model where services are unbundled and paid for separately, often found in health care.

Fiduciary Duty: The highest standard of care. Someone with a fiduciary responsibility must make the best decisions available for his or her client.

Finance Charge: The total cost of credit, including interest and fees but not charges incurred in a comparable cash transaction.

Fixed Annuity: An investment contract sold by an insurance company that guarantees fixed payments, either for life or a fixed period. *See* ***Annuity***.

Fixed Interest Rate: An interest rate that stays the same for the life of the loan.

Foreclosure: The legal process required for a lender to take ownership of a home pledged as collateral.

Grace Period: A period of time specified in a loan contract, during which default or cancellation will not occur even if a payment is due.

Gross: Without tax or contributions being deducted.

Hard Pull: *See* ***Inquiry (Hard Pull)***.

Health Maintenance Organization ("HMO"): A health insurance organization to which subscribers pay a fee in return for a range of medical services.

Hold: The temporary unavailability of money in an account.

Homeowner's Insurance: Insurance designed to protect an individual's home against damages, or against damage to possessions in the home.

Individual Retirement Account ("IRA"): A type of retirement account that allows individuals to direct pretax income towards investments, which can grow tax-deferred

Inflation: A rise in the general prices of goods and services that lowers the purchasing power of money.

Inquiry (Hard Pull): When a creditor accesses an individual's credit history. A "hard pull" generally results in a dip in a consumer's credit score for a limited period of time.

Installment Credit: Credit offered for a fixed term and, if the interest rate is fixed, a fixed monthly payment.

Insurance Policy: A document detailing the terms and conditions of an insurance contract.

Insurance: A contract providing protection against a possible eventuality, often a financial loss.

Installment Credit: A sale made under the agreement purchased goods or services will be paid for in a series of payments made over a set period of time.

Interest: Money paid for use of money lent, or for delaying debt repayment.

Junk Bond: A type of high-yield, non-investment-grade bond. *See* ***Bond***.

Late Fee: A fee charged by a creditor when a borrower fails to make a timely payment.

Lender: An individual or entity that makes funds available for others to borrow.

Life Insurance: Insurance that pays a sum of money on the death of the insured person or after a set period.

Line of Credit: A loan arrangement in which a financial institution allows a customer to borrow funds up to a specified amount.

Loan Term: The period of time within which payments on a loan must be made.

Managed Health Care Plan: A health care plan which requires individuals receive services from specific providers that are part of the plan.

Maturity: The final payment date of a loan or other financial instrument.

Medical Payment Coverage: A type of automobile insurance that insure drivers and passengers against medical or funeral expenses resulting from an accident.

Money Market Account: An account that pays interest based on interest rates in money markets.

Mutual Fund: A professionally-managed diversified investment program funded by shareholders.

Negotiable Instrument: A document guaranteeing the payment of money, with the payer named on the document.

Negotiable Order of Withdrawal ("NOW"): A bank account with which the customer is permitted to write drafts against money held on deposit.

Net: Gross, minus taxes and/or contributions.

Non-Sufficient Funds Fee ("NSF"): A fee assessed if an account does not have enough money available to cover a transaction.

Open Enrollment: A period of time set by an insurance company (or employer if through group insurance), during which individuals can purchase health insurance or change existing policies.

Open-End Credit: A pre-approved loan that allows one to draw upon a line of credit up to a set limit. Open end credit may be repaid prior to payments coming due. *See* ***Revolving Credit***.

Out-of-Pocket Limit: The maximum amount a consumer must pay during an insurance policy period for health care services.

Overdraft Fee: A fee charged to a consumer, if the individual withdraws funds from an account that does not contain enough money to cover the withdrawal.

Overdraft Line of Credit: A line of credit attached to a checking account, which covers overdrafts.

Overdraft Protection: *See* ***Overdraft Line of Credit***.

Passbook Loan: A loan extended to a savings account holder, in which the balance of the savings account serves as collateral for the loan.

Payday Loan: A small, short-term unsecured loan.

Personal Loan: An unsecured loan established for personal use, often to fill gaps in a consumer's income. Personal loans typically range from $500-$5000, and feature relatively high APRs.

Preferred Provider Organization ("PPO"): A managed care organization whose providers have agreed with an insurer or administrator to provide health care at reduced rates to the administrator's clients.

Preferred Provider: A health care provider that is part of a preferred provider organization.

Preferred Stock: Stock that entitles the holder to a fixed dividend. Preferred stock dividends take priority over common-stock dividends.

Premium: A fee to obtain an insurance policy. Premium costs are influenced by several factors including, but not limited to, the type of insurance, the amount of coverage, and personal characteristics.

Principal Balance: The balance of a debt, not including interest.

Private Health Insurance: Health insurance plans offered by the private health insurance industry.

Property Damage Liability Coverage: Automobile insurance that covers the cost of damages to someone else's property after an accident caused by the policyholder.

Provision: A condition or requirement in a legal document.

Ratify: To give formal consent.

Replacement Cost: The cost to replace an insured property.

Repossession: When a creditor takes possession of collateral from a buyer who is in default on a loan.

Residential Property: Property used as, or suitable for use as, a dwelling.

Returned Check Fee: A charge assessed on a consumer's account if a check is returned unpaid.

Revolving Credit: Credit requiring monthly payments of less than the full amount due. The balance not paid in full is generally subject to a finance charge.

Right-to-Cure Notice: A notice, from a creditor to a borrower, notifying the borrower her or she missed a payment, and informing them the creditor may exercise rights under the law, including repossession or the start of foreclosure, unless payment of all past-due amounts is made by a specified date. Right-to-cure notices remain effective for 12 months after the original date sent.

Routing Number: A unique numeric code which identifies a financial institution.

Savings Account: An interest-earning bank account.

Savings and Loan Association: A financial institution that accepts savings and lends money, chiefly for home mortgage loans. Savings and loan associations may also offer checking accounts and other services.

Savings Bank: A financial institution that receives savings accounts and pays interest to depositors.

Secured Loan: Loans in which a security interest in property is pledged.

Share Account: An account held at a credit union.

Share Certificate: A document signed on behalf of a corporation, which serves as proof of ownership of a number of shares of stock.

Simple Interest: An interest calculation based only on the original principal amount of a loan.

Stock: A type of security which signifies partial ownership in a corporation, and a claim on part of the corporation's assets.

Statute of Limitations: A statute prescribing a period of limitation for the bringing of certain kinds of legal action. In Maine, the statute of limitations on debt is 6 years.

Student Loan: A loan taken out to pay for educational expenses.

Tax Credit: An amount of money that can be offset against a tax liability.

Tax Lien: A legal claim on property for unpaid taxes.

Taxable Income: Income used to calculate income tax due.

Term: The number of years or months during which the loan must be repaid.

Term Life Insurance: Life insurance that pays a benefit in the event of the death of the insured during a specific term.

Term Rider: An attachment to a life insurance policy that provides additional term coverage.

Thrift: *See* ***Savings and Loan Association.***

Trade-In: A used vehicle accepted by a retailer as partial payment for another vehicle.

Tradeline: An entry on a credit report made by a creditor describing the details of a consumer's account, including status and activity.

Treasurer's Check: *See* ***Cashier's Check.***

Underinsured Motorist Coverage: An automobile insurance policy that extends coverage to include damage caused by a motorist with insufficient insurance.

Uninsured Motorist Coverage: An automobile insurance policy that extends coverage to include damage caused by a motorist without insurance.

Universal Life Insurance: Life insurance that combines term life coverage with savings invested in a tax-deferred account.

Unsecured Loan: A loan where no collateral is pledged.

Usury Law: A law that sets limits on maximum allowable finance charges.

Variable Annuity: An annuity in which payout is based on a guaranteed number of units.

Variable Interest Rate: An interest rate which fluctuates over time.

Volatility: The fluctuation in value of investment tools.

Wage Garnishment: The practice of withholding a portion of a borrower's wages, without his or her consent.

Whole Life Insurance: Life insurance that pays a benefit on the death of the insured, and also accumulates a cash value.

Publications

Be sure to check out other free booklets from the
Bureau of Consumer Credit Protection:

Downeaster Common Sense Guide: Automobile Buying and Financing – From calculating "how much vehicle" you can afford, to vehicle research, shopping for the best APR and deciding on the best loan term for your needs, this booklet is a comprehensive guide to purchasing and financing a vehicle.

Downeaster Common Sense Guide: Credit Cards—Paper or Plastic? – This comprehensive booklet addresses credit cards: how they work, their responsible use, how to comparison shop for a credit card, when to pay cash, use a debit card charge on a credit card and what to do if you fall behind on your credit card payments.

Downeaster Common Sense Guide: Credit Reports and Credit Scores – Learn the basics of credit, gain insight into how credit reporting and scoring work, and discover the impact your credit has on your ability to borrow with this publication from the Bureau of Consumer Credit Protection.

Downeaster Common Sense Guide: Debt Collection – If you are past due on your credit card, mortgage loan, auto loan or student loan, this is the FREE booklet for you! Learn about your rights in a consumer debt collection action, and how to deal with collectors. This booklet also provides guidance in spotting prevalent debt collection scams and contains ample "cease contact" and "debt validation" letters.

Downeaster Common Sense Guide: Finding, Buying and Keeping Your Maine Home – This guide is a resource for first time homebuyers, and provides an overview of the mortgage lending process, types of mortgage lenders and loans, and other related topics.

Downeaster Common Sense Guide: Gone Phishing – Identifying and Avoiding Consumer Scams – This guide is all about helping consumers defend themselves against being scammed. It details tactics and hooks used by scammers, offers advice to consumers so they can protect themselves, and explains how to report the scams to authorities.

Downeaster Common Sense Guide to High Interest/High Cost Loans – Not all loans are created equal! This booklet provides valuable information on some of the most expensive types of loans, and how to avoid falling into too much debt if you choose to use them.

Downeaster Common Sense Guide to Student Loans – A comprehensive guide for the prospective college student on the world of educational loans. This book covers educational loan types, the FAFSA process, how to apply for scholarships and grants, and the rights of a student debtor in the repayment/collection process. A must read for college-bound students and their parents!

Downeaster Guide to Elder Financial Protection – The "how-to" guide for Maine seniors who are interesting in stopping unwanted telemarketing calls, pre-approved credit offers, and junk mail. This guide has sections on how to stop identity theft and how to recognize and stop elder scams and financial exploitation.

These guides are free to Maine residents. Out-of-state orders are $6.00 each, or at a volume discount of $4.00/copy on orders of 50 or more (shipping included).

To order, call 1-800-332-8529 (in-state) or 1-207-624-8527 (outside of Maine).

EQUIFAX Experian TransUnion.

Annual Credit Report Request Form

You have the right to get a free copy of your credit file disclosure, commonly called a credit report, once every 12 months, from each of the nationwide consumer credit reporting companies, Equifax, Experian and TransUnion.

For instant access to your free credit report, visit www.annualcreditreport.com.

For more information on obtaining your free credit report, visit www.annualcreditreport.com or call 877-322-8228.

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[illegible]

[illegible]

First Name | M.I.

Last Name | JR, SR, III, etc.

Current Mailing Address:

House Number | Street Name

Apartment Number / Private Mailbox | For Puerto Rico Only: Print Urbanization Name

City | State | ZipCode

Previous Mailing Address (complete only if at current mailing address for less than two years):

[illegible]

[illegible]

[illegible]

Consumer Protection Resources

Maine Bureau of Consumer Credit Protection	1-800-332-8529 TTY Maine Relay 711
Maine Bureau of Insurance	1-800-300-5000 TTY Maine Relay 711
Maine Bureau of Financial Institutions	1-800-965-5235 TTY Maine Relay 711
Maine Office of Aging and Disability Services	1-800-262-2232 TTY Maine Relay 711
Maine Office of the Attorney General (Consumer Hotline)	1-800-436-2131 TTY 1-207-626-8865
Maine Office of Professional and Occupational Regulation	1-207-624-8603 TTY Maine Relay 711
Maine Office of Securities	1-877-624-8551 TTY Maine Relay 711
Maine Public Utilities Commission (Consumer Assistance Division)	1-800-452-4699 TTY 1-800-437-1220
Maine Real Estate Commission	1-207-624-8524 TTY Maine Relay 711
Legal Services for the Elderly	1-800-750-5353 TTY Maine Relay 711
Commodity Futures Trading Commission	1-866-366-2382
Consumer Financial Protection Bureau (CFPB) Consumer Hotline	1-855-411-2372 TTY 1-202-435-9742
Federal Reserve Consumer Hotline	1-888-851-1920
National Credit Union Administration (NCUA)	1-800-755-1030
Federal Trade Commission Consumer Response Center	1-877-382-4357
Federal Trade Commission ID Theft Hotline **(after dialing, press "0" to reach a live operator)**	1-877-438-4338
Internet Crime Complaint Center (IC³)	www.ic3.gov
U.S. Department of Veterans Affairs	1-800-729-5772
U.S. Postal Inspection Office — Ask for the Portland, ME Field Office	1-877-876-2455

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Bureau of Consumer Credit Protection

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www.Credit.Maine.gov

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