Financial Management

Working for Wisconsin Families
Extension

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4 STEPS TOWARDS BEING DEBT FREE

1. Identify the debt you owe.
Identify the debt you owe. Make a list of all your debt, including four items: the name of your creditor, the total amount you owe, the rate of interest you are being charged and the amount you pay each month towards this debt, if any.

2. Stop Creating Debt
The first step in successfully paying off debt is to stop creating debt.

Example 1

Name	Total Amt Owed	Percent	Monthly Payment
VISA	$2,000.00	18%	$50.00

A. Create savings strategies for non-monthly expenses. For example, car insurance or water bills may be paid quarterly. Set 1/3 of the quarterly bill aside each month.
B. Increase income and decrease expenses so you have more money for unexpected expenditures.
C. Develop a strategy to decrease impulse spending.
   i. Do not carry your credit cards with you.
   ii. Make a plan before making a purchase. Make a list of items you intend to purchase, identify an amount you intend to spend, and if you are going to charge these items develop a plan for how you will repay this debt.
   iii. Discuss your intent to use your credit card with another person to help you brainstorm other alternatives.
   iv. Give yourself a 24-hour "cooling off" period before making a purchase.

3. Determine how much money you have each month to put towards debt repayment.
Once you develop your spending plan, you can determine the amount you have to put towards debt repayment by subtracting the amount needed for total monthly expenses (not including debt) from your total net monthly income (income after payroll deductions). If you have additional monthly saving goals, subtract this amount also from the total net monthly income. The remaining amount is the monies (money?) you have available for debt repayment.

Total Monthly Income $1200– Total monthly expenses $1000= $200 (for monthly debt repayment)

Often debt collectors will try to get you to agree to a repayment plan that is not realistic for your financial situation. Determining a realistic amount for debt repayment will empower you.

4. Apply one or more of the following Debt Repayment Strategies

Strategy #1 The Power of Negotiation

Find an alternate creditor that offers a lower rate. Not just 6-month offers, but also a permanent rate, for the life of the loan or credit card.
Then call your creditor and tell them you are tempted to transfer your balance to another creditor and ask them if they would consider decreasing your interest rate to keep you as a customer. It doesn't hurt you to make the call, even if they say no.

For example, if you are paying 24% interest on your

MasterCard you may want to transfer the balance of what you owe MasterCard to your Visa card, where you are only paying 18%.

Name	Balance	Monthly Pymt.	%	Time to Pay off	Interest Paid
MC	$3,000	$80	24%	5 yrs. 11 months	$2,600.00
VISA	$3,000	$80	18%	4 yrs. 8 months	$1,442.12
Savings by Reducing Interest Rate			6%	1 yr. 3 months	$1,157.88

Be cautious in your attempt to lower your interest rate that you do not apply for a new loan or credit line that may deny you. Denials of credit are a negative mark on your credit report. Also, too many inquiries into your credit history by creditors could possibly have a negative affect on your credit score. To avoid these kind of problems, always tell a lender or creditor what your financial situation is and ask them upfront if you fit their criteria before actually applying for new credit. If you transfer your balance to another card, be sure to destroy the old card. This removes temptation to rebuild new debt.

Strategy #2 Maintain Level Payments

The strategy of maintaining level payments is to maintain the same level of payment even when the total amount due decreases. So if your debt payment is $80 a month, you keep paying $80 a month toward your debt even when minimum payments decrease to $65 a month.

Here's how this works. If you paid off a credit card debt of $3200 with an interest rate of 14.9%, using the traditional minimum payments the credit card requested, it would take you 18.5 years to pay off this debt and you would have paid $2919 in interest. Using the strategy of maintaining level payments you would have started your payments at $80 a month and maintained paying $80 even when the minimum payment decreased. You would pay off your loan in 4.8 years and only pay $1259 dollars in interest. The tool PowerPay utilizes this strategy.

You can access PowerPay on the web: http://www.extension.usu.edu/powerpay

Balance	Interest Rate	Method	Time to Pay	Amount of Balance
$3200	14%	Minimum Pymts.	18.5 yrs.	$2919
$3200	14%	Maintain Level Pymts.	4.8 yrs.	$1259
Savings using Maintaining Level Payments			13.7 yrs.	$1660

Strategy #3 Consistently Pay More Each Month

Consistently paying a little extra each month, over time, can make a big impact on your debt**.**

Mortgage loans are a great way to demonstrate how this works. SEE www.choosetosave.org for online calculators.

Credit Card Examples:

Name	Amt. owed	%	Monthly pymts.	Time to pay off	Int. Paid
VISA	$4,900	14.4	$140.00	3 yrs. 10 months	$1,493
VISA	$4,900	14.4	$170.00	3 yrs.	$1,149
Savings using consistently paying more				10 months	$374

If you have a mortgage for $70,000 at 8% for 30 years and you pay $50 more a month, you will pay off your mortgage 8 years sooner and save yourself $36,000 in interest.

Of Course The Most Powerful Affect On Debt Repayment Is Combining Strategies

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