

Debt Repayment Strategies

Strategy #1: The Power of Negotiation

Look for another credit card that offers a lower rate than your current credit card. Be sure it is not just a short-term introductory rate, but a lower rate that will continue as you use the card. Then call your current credit card company to ask them if they will match that lower interest rate to keep you as a customer. It doesn't hurt you to make the call, even if they say no. If they say no, transfer the amount you owe on the credit card with a higher interest rate to the new credit card with the lower interest rate. For example, if you are paying 24% interest on your MasterCard you may want to transfer that balance to your Visa card with an 18% interest rate. However, before making the transfer, read the contract and look for hidden fees.

Name	Balance	Monthly Pmt.	%	Time to Pay Off	Interest Paid
MasterCard	\$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

Strategy #2: Maintain Level Payments (Power Payments)

The key to this strategy is maintaining the same amount of payment even as the total amount due decreases. For example, 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 \$3,200.00 with an interest rate of 14.9% by making the minimum payments the credit card requested, it would take you 18.5 years to pay off this debt and you would have paid \$2,919 in interest. Using the strategy of maintaining level payments you continue making payments of \$80 a month even when the minimum balance decreased. As a result you will pay off the debt in 4.8 years and pay \$1,259 dollars in interest, saving \$1,660.

Balance	Interest Rate	Method	Time to Repay	Interest Paid
\$3,200	14.0%	Minimum Pmts.	18.5 yrs	\$2,919
\$3,200	14.0%	Level Pmts.	4.8 yrs.	\$1,259
Savings using Maintaining Level Payments:			13.7 yrs.	\$1,660

Strategy #3: Consistently Pay More Each Month

By consistently paying a little extra each month you can make a big impact on your debt. This is especially true for longer-term debts like mortgages.

Mortgage loans are a great way to demonstrate how this works. If you have a \$70,000 mortgage at 8% for 30 years and you pay \$50 more a month, you will pay off your mortgage 8 years sooner and save over \$35,000 in interest.

Name	Amount Owed	%	Monthly Pmt	Time to Repay	Interest Paid
Mortgage	\$70,000	8	\$ 514	30 years	\$114,500
Mortgage	\$70,000	8	\$ 554	22 years	\$ 79,130
Savings by Consistently Paying More:				8 years	\$ 35,370

Credit Card Example:

Name	Amount Owed	%	Monthly Pmt	Time to Repay	Interest Paid
VISA	\$4,900	14.4	\$ 140	3 yrs. 10 months	\$1,493
VISA	\$4,900	14.4	\$ 170	3 yrs.	\$1,149
Savings by Consistently Paying More:				10 months	\$ 374

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

Pitfalls and Traps of Other Debt Strategies

1. Restructuring Your Debt

A. Consolidation Loans. These loans take several debts and consolidate them into one loan, preferably with a lower interest rate. This can decrease your monthly payment and often reduce the overall amount of interest you are paying. A consolidation loan can be a good idea for people who already can pay their monthly bills and just want to be more efficient with debt repayment. You need to have good credit and collateral in order to get a consolidation loan without paying excessive interest.

Pitfalls and Traps:

- **Recycling Debt**

When people who are having trouble managing their money consolidate their debt, they often recycle their debt--continue to create debt. That's because they haven't changed any behaviors. People may intend to change but once the pressure and stress of the debt is reduced through the consolidation, the motivation to change is gone.

- **Increase Risk or Cost of Credit**

Often people want to use equity on their home to repay debt. They do this because they have no other collateral for a consolidation loan. Failure to make payments on a home equity loan puts their home at risk. They have increased their risk by converting unsecured debt (credit card debt-- debt not secured by any property) into a secured debt. They also have increased the amount of interest they will be paying and perhaps the length of time they will pay off their debt.

B. Refinancing Your Home

People refinance their homes to take advantage of lower interest rates or to decrease their monthly payment. Sometimes it is done to create extra money for purchases (like a car) or debt repayment. This type of "cash-out refinance" adds to the total debt and increases the time and cost of repaying the loan.

Pitfalls and Traps:

- **Affect on retirement**

Consider the age of the person thinking of refinancing and the impact this may have on paying off their home before retirement.

- **Costly**

If they do this often it can be very costly and they will make little headway on paying off principle.

C. Transferring balances

Another way to consolidate debt is transferring balances from one credit card to a lower interest credit card. Be careful, read the contract.

Pitfalls and Traps:

- Some creditors are charging balance transfers at the same rate of a cash advances.
- Look at contract for a provision that states if you fail to meet any aspect of the contract including being one day late on a payment, the interest rate is increased dramatically with a contingency that there will never be the option of reducing it.
- Sometimes the billing cycle is too short to comply with timely payments.
- Be aware of the cost of extra charges: late fees, over limit fees, cash advance fees, yearly fees.
- If you switch balances often you may be stretching out the time it will take to pay off your debt.

D. Use a Credit Counselor to Negotiate Debt

A non-profit consumer credit counseling agency may be able to negotiate a debt management plan with your creditors. This often includes reduced interest rates, lower monthly payments and consolidates them into one monthly payment. Costs are usually based on your ability to pay. In Wisconsin the initial setup fee is limited to \$50 or \$25 if you sign up for a debt management plan. Monthly fees vary so check costs before signing an agreement. In Wisconsin the maximum monthly fee can't exceed 10% of the money sent to creditors or \$120, whichever is less. Check your phone book to find a consumer credit counseling service in your area. Four national debt phone counselors are:

Myvesta.org	1-800-680-3328
Consolidate Credit Counseling Services	1-800-728-3632
Money Management International	1-800-762-2271
Consumer Credit Counseling Services (CCCS)	1-800-388-2227

Pitfalls and Traps:

- If a repayment plan cannot be accomplished in three to five years, usually this is not an option.
- Debt repayment plans that decrease interest or monthly payments will show up on credit reports as late or reduced payments.
- It can be expensive, especially if you have several creditors and the fee is based on the number of accounts in your debt management plan.
- There are disreputable companies claiming to do credit counseling, so choose carefully. They could overcharge for their services. Others may take your money and not pay your creditors, or they may not even have called your creditors. Many states, including Wisconsin, require licensure of credit counseling agencies that do business in the state.

2. File Bankruptcy—the Last Resort

There are two common consumer bankruptcies-- Chapter 7 (liquidation) and Chapter 13 (restructuring debt). In a Chapter 7 bankruptcy, you surrender all

your property that is not exempt so it can be sold to pay off your debts. Any debt that's dischargeable is then discharged (forgiven). A Chapter 7 bankruptcy remains on your credit report as a negative mark for 10 years. You are not allowed to file again for 6 years. Chapter 13 bankruptcy sets up a court-supervised plan for you to pay back your debt over a 3-5 year period. Debt that remains is then discharged. A Chapter 13 bankruptcy remains on your credit report for 7 years. You can file a Chapter 13 bankruptcy as often needed, once the previous one is completed. Both kinds of bankruptcy have a fee; a Chapter 13 is usually more expensive. Fees run from \$500-\$1500 depending on the complexity of the filing. In most cases attorneys will require their fee up front.

There are assets that are exempt from bankruptcy, such as your home as long as you agree to continue making your mortgage payments. You are allowed one vehicle and some personal property. The value of these items is determined at a state and federal level. Each has its own guidelines. Certain debts are protected from bankruptcy, for example you must continue to pay alimony, student loans, child support, and back taxes.

Unclaimed debt cannot be attached later. You must claim all your debt when you file. If you forget something you cannot include it once the bankruptcy is started. Timing is everything. Do not look to your bankruptcy attorney to determine the best time to file. Your accountant or bookkeeper is a better judge. If you have pending debt, like future hospital bills, now may not be the best time to file. You can't file again for six years.

Bankruptcy is a specialized law practice; use a qualified attorney. Questions for selecting a bankruptcy attorney:

How long have you been handling bankruptcy cases?

About what percent of your business is bankruptcy?

What will be the total cost of this bankruptcy?

Will I have extra charges later on that are not included in the original fee?

Pitfalls and Traps:

- **Consequences of filing bankruptcy**

It can be difficult to rent or obtain employment if a credit check is required. It can be difficult to borrow money from a financial institution. Loans that are approved will have a higher rate of interest.

- **Recycling**

Behavior must change or debt will reoccur. Often people file bankruptcy and then turn around and start to incur more debt.

- **Determining if it's the best option**

A bankruptcy attorney will almost always recommend bankruptcy if a person is eligible. They do not determine if this is the best option for a client. They also do

not address behavioral changes that might put them at risk after the debt is discharged.

- **Shame**
Often people who file bankruptcy feel ashamed and it is kept a secret. This can be a heavy burden to carry.