DEBT Reduction Services

A real solution.

NATIONAL FINANCIAL EDUCATION CENTER

DEBT

Financial Toolbox

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1. Signs of Financial Trouble

It seems to be human nature to think that we can clearly see and understand other people's problems, yet we often fail to recognize our own challenges. The way we deal with our money is no exception.

Here's a list of situations and behaviors that, if you recognize them in your own life, call for your attention and time. Some may be alarming, others worrisome, and still others simply concerning.

- You find it "impossible" to save ANY money, month after month.
- You make ONLY the minimums payments on all of your loans, including mortgage, auto, and credit cards.
- You have either recently considered or have recently used the services of a payday lender, title loan company, a pawn shop, a rent-to-own business, or have opted for a tax refund anticipation loan.
- You "float" checks for bills by sending them off in the mail BEFORE you have the actual money in your checking account to cover the amount due.
- You have no idea what your current credit card balance might be.
- You use your credit card regularly but don't know what your credit limit is.
- You borrow money from family or friends to cover the costs of your "basic" expenses.
- You work overtime just to cover the costs of your "basic" expenses.
- You use a credit card, cash advance, or other expensive loan to cover the costs of your "basic" expenses.
- Twenty percent (20%) or more of your take home pay is going toward just the minimum payments on your loans (excluding primary residence mortgage).
- You put off going to a physician, dentist or other health professional because of your financial situation.
- You keep yourself up at night worrying about your finances.

So what should you do if you recognize any of these signs in your own finances? Here are a few ideas:

1. If you're not sure, then don't be afraid to ask for help. You'll find that those who are successful with their own finances are, far more often than not, very willing to share some time with you.
2. Find a local nonprofit organization, such as the National Financial Education Center at Debt Reduction Services Inc, that provides free financial management classes.
3. Contact a member of your state's Jump$tart Coalition for Personal Financial Literacy® and ask about any classes or mentors that they may have available.
4. Spend time working on your finances. Millionaires spend an average of four hours every week working on their personal finances. They started that habit BEFORE they acquired their wealth, not after. They are financially successful BECAUSE they were already in the habit of regularly paying attention to their money.

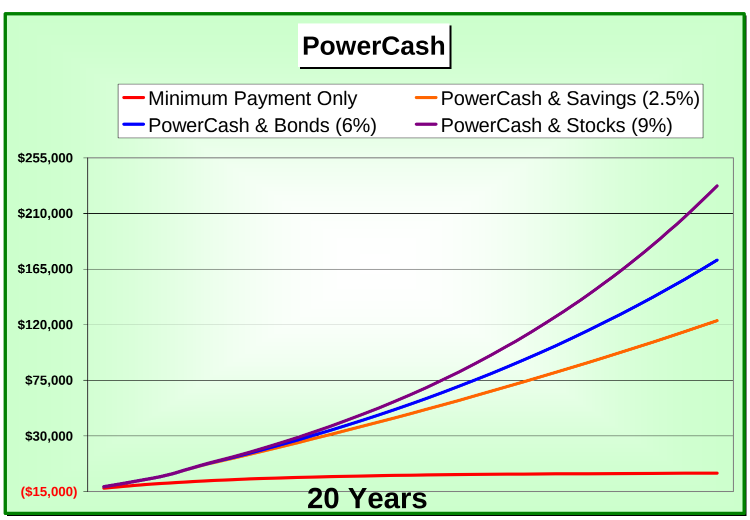
2. Debt Management

PowerCash™

Generally, financial experts find that for most of us, 20% of our expenses are unaccounted for. Much of these "unidentifiable" expenses likely take the form of the individual's "Budget Busters" – the small purchases of $1-5 a day that we don't track – "because it's just a few dollars." Consequently, most individuals have "extra" money to add to their debt elimination payments, but they're spending it without a plan. To "uncover" the surplus money in your budget, work through the Power Cash Rule below:

1. You must have a budget and understand where your money has really gone in the previous one to three months.
2. Determine what you spend each month on controllable (discretionary) expenses, such as entertainment, groceries, clothing, and dining out.
3. Multiply that total amount by 10%. This is your "**POWERCASH**."
4. Take out of your paycheck the "**POWERCASH**" by either transferring it to your savings account, adding it to your monthly debt repayment, or a combination of the two. For a family of 4 that spends $600 a month on groceries, $150 a month on eating out, $100 a month on entertainment, and $50 a month on clothing, the **POWERCASH** Rule would add $90 each month to their savings or their debt elimination payment.
5. More likely than not, you will hardly notice the difference between living on 100% of your available income and the amount left over after taking out your **POWERCASH**.
6. When repaying debt, commit to never decreasing the monthly payment until your debt is eliminated. Once an account is paid in full, take the amount you were sending to that company and apply it to another account. This is known as "Snow Balling" your payments.

The following chart demonstrates the results of regularly adding $50 in **POWERCASH** to the current minimum payment on a $15,000 credit card balance with an APR of 14.9%.



Minimum Payments Only: Paid off after 20 years and an extra $10K in Interest!
PowerCash to Pay Off then into Savings: Paid off in 3 years then builds $123K in savings (includes $25K of Interest Earned)!
PowerCash to Pay Off then into Bonds: Paid off in 3 years then builds $172K in Government Bonds (includes $74K of Interest Earned)!
PowerCash to Pay Off then into Stocks: Paid off in 3 years then builds $232K in savings (includes $134K of Interest Earned)!

PowerCash™ Calculator

Determine how much you usually spend each month for the expenses in rows #1-7. Write those totals in the second column. Think of other types of expenses you have each month that you have some control over (either in how much you purchase or how much you use). Insert them in second column for rows #8-10.

Add up the amounts in the second column and write the total in row 11.

Multiply row 11 by 10% and enter the result in row 13. **This is your PowerCash**!

Consider splitting your PowerCash each month into three goals: paying down debt, building an emergency savings plan, and growing your long-term investments.

#	**CONTROLLABLE EXPENSE**	**HOW MUCH I SPEND EACH MONTH**
1	Groceries:	
2	Entertainment:	
3	Dining Out:	
4	Habits/Hobbies:	
5	Gifts/Donations:	
6	Travel/Fuel/Transportation:	
7	Other:	
8	Other:	
9	Other:	
10	Other:	
11	Total of My Monthly Controllable Expenses	=
12		X 10%
13	**MY POWERCASH**	=

Prioritizing Your Debt to Accelerate Repayment

Not all debts are created equal, nor should you accord all debt payments equal importance. Additionally, when determining a debt repayment method, we need to match our debt repayment method to our type of personality. Not all methods work for all people.

EACH of the methods described below have ALL of these points in common:

1. The minimum payment on all accounts is made on time.
2. You make a list of all of your debts, with the top priority debt on the top.
3. PowerCash is added to the debt listed as top priority on your list.
4. Once a debt is paid off, its monthly payment is added to the monthly payment of the debt at the top of your list. In other words, from start to finish, the total amount of repayments you send each month does not change, even when the creditors offer lower payments.
5. Sit back and enjoy watching your debt disappear faster than you thought possible.

Now, ask yourself, which of the following methods is most likely to work best for me?

Accelerated Debt Repayment Methods

1. *By Importance of Debt*. Debts that are “secured” against some type of property, such as vehicles, real estate and your mortgage, should top everyone’s list. Make sure that the minimum payment on these accounts is made every month without fail. If you risk making a late payment or missing payment all together on these accounts, getting current and caught up will usually take precedence over all other payments. Once that’s understood, you can put these payments in their proper place according to which of the following accelerated repayment methods fits you best.
2. *By Interest Rate: Highest to Lowest*. Organize your debts with the highest interest rate at the top of the list. Sending your PowerCash first to the debt with the highest interest rate until it’s paid off, then working down, will ensure that you pay the least amount of interest over all. NOTE: This method is recommended by most financial experts, but it generally requires greater discipline and more patience than the next method.
3. *By Balance: Lowest to Highest*. Organize your debts with the lowest balance at the top of the list. Sending your PowerCash first to the debt with the lowest balance means that you’ll be more likely to see a debt paid off sooner than if you used the Interest Rate method above. For many, if not most of us, seeing debts paid off sooner (even if it’s a debt with a low interest rate) can provide us with the motivation we need to continue adhering to our accelerated debt repayment plan.

Finally, if you require further motivation, consider throwing yourself a debt repayment party after each debt is paid off. However, use no more than half of the monthly debt payment that you just got rid of. You may even consider using such an idea as incentive if you’re married and your spouse is not committing to the process.

Debt Repayment Worksheet

Why I/we want to be out of debt? ____

	Creditor's Name	Creditors Phone	Account Name	Current Balance	APR	Current Minimum Payment	Monthly Due Date
EXAMPLE							
	Visa	(555) 555-1212	Jim's Visa	$2,010	19.9%	$60.30	21st
1							
2							
3							
4							
5							
6							
7							
8							
9							
10							

3. Outside Help

13 FAQs about Credit Counseling

1. **What does a Credit Counseling Agency do?**
Credit Counseling Agencies (CCA) provide education and assistance to consumers who have more debt than they feel they can repay on their own. CCAs negotiate concessions from creditor(s) to reduce or eliminate interest charges and stop late and over-limit fees. If they are nonprofit (most are), they will also provide free education materials and/or courses on basic money management.

2. **Who should consider seeing a Credit Counselor?**
Credit counseling is appropriate for individuals who are trying to pay off their debt *Dollar-for-Dollar* but who don't feel they are making any headway on their own. They may also be individuals who have high interest rates on their credit cards, who may have taken out a payday loan, and/or who may be late on any such debts. Credit counselors may not be able to help you with the renegotiation of a mortgage, car loan, or other secured debt. For help with your mortgage, see a HUD-certified counselor (www.hud.gov).

3. **What are the cost and fees involved in Credit Counseling?**
There is no fee for meeting with a credit counselor to discuss your situation. Fees are generally only charged if you sign up on what is commonly referred to as a Debt Management Program (DMP). When enrolled in a DMP, your debt payments are consolidated into one monthly payment to the credit counseling agency who then distributes them to your various creditors on your behalf. There is usually an initial DMP Enrollment fee (typically $75 or less) and monthly administrative fees (generally capped at $50 or so). These may be flat fees, but they are more often based on a percentage of your monthly debt payment to your creditors or the number of creditors you place on the program. Just make sure that you get a written contract and that it specifies all of your financial obligations.

4. **Is Credit Counseling the same as Debt Consolidation?**
No. The term "Debt Consolidation" usually refers to the practice by a lender of consolidating multiple loans into one loan with one payment. Effectively, the new loan is used to pay off the other loans. Credit Counseling utilizes a Debt Management Program that only consolidates the payments into one, but not the debts.
There are several potential pitfalls involved in debt consolidation. First, debt consolidation loans are not very easy to qualify for. Second, the interest rates on such loans tend to be fairly high. Also, if an individual does qualify for a debt consolidation loan, there quite likely will be new loan fees involved. It's important to note that debt consolidation is just shuffling debt around and may not actually reduce debt in the near or long term.

5. **Does meeting with a Credit Counselor impact my credit score?**
No. Credit counselors do not report your visits or counseling sessions to any credit bureau. Only if you sign up for a Debt Management Program through the credit counselor is there any notation at all on your credit report. See the next question.

6. **How does participating in a Credit Counseling program impact my credit score?**
   Fair Isaac Company, the pioneer in credit score modeling and still the overwhelmingly most commonly-used credit score, clearly states that they do not take participation in a credit counselor's debt management program into account when calculating an individual's credit score. It should be noted, though, that any of the following may occur:
   *Creditors may place a temporary notation on the individual's report stating that they are enrolled in a DMP. This is done for the purpose of preventing any further credit card accounts from being opened while the individual is paying off current debt. The creditor is obligated to remove the notation once the individual is no longer enrolled in the DMP.
   *When an individual enrolls in a DMP, their accounts are effectively closed (either by the individual or by the creditor) and converted into monthly installment accounts by the creditor. Because of how a credit score is calculated and depending upon the balance on the individual's account(s), such closings may initially lower the individual's credit score. However, FICO's credit scoring model relies most heavily upon a history of on-time payments and lower balances, which is also what we strive to help our clients achieve.
7. **How long does it take to pay off debt through a DMP?**
   DMPs, by regulation, cannot project debt repayment past 5 years. Most DMP clients who complete the program pay off their debt within three to five years.
8. **How much debt does an individual have to have to participate in a DMP?**
   Most legitimate credit counselors do not set limits on the how little or how much debt clients must have to enroll in their Debt Management Program.
9. **What are the steps to signing up on a DMP?**
   First, an individual contacts the Credit Counseling Agency and goes through a no-obligation credit counseling session to determine if the individual is in position to repay creditors on their own, through a DMP, or if it might be more appropriate to refer them to a bankruptcy attorney. The individual and the counselor look over the household budget and the circumstances of the individual's debt. If the counselor and the individual agree that enrolling in a DMP will be beneficial, then the individual completes the enrollment agreement, pays the enrollment fee, and signs up for automated monthly payments through their checking account. After that, it is the individual's responsibility to ensure there are sufficient funds to cover the set monthly payment. It is the Credit Counseling Agency's responsibility to work with the creditors on the proposed program, draw the funds, disperse them to the creditors within just a few days, and provide superior customer service.
10. **Rather than signing up for a DMP, shouldn't I just use the equity in my home to pay off my credit card debt?**
   As we've seen in recent years, a falling real estate market can present various financial dangers to homeowners in general. It may also completely erase the equity the owner has in the home. Still, as lenders are quick to point out, there are some tax advantages to using a home equity loan or line of credit to pay off high-interest credit card balances. However, what such lenders usually ignore or fail to mention is that in about 70% of all such cases, the borrower will, within just one to two years, use those same paid off credit cards to build their debt back up to their original

balances… at the same time that they will have a home equity payment due each month. When an individual purchases a pizza with a credit card and then pays that credit card off with a home equity loan, they are effectively putting their home at risk of foreclosure because of a pizza. Failing to pay a home equity loan may very well lead to foreclosure.

11. **What happens if I start a DMP and have to quit mid-program?**
Because of certain regulatory issues, creditors may not be able to offer the individual more DMP concessions within the next five years. Or, they may return the individual's credit card accounts to their previous interest rates. There are no penalties charged by the Credit Counseling Agency.

12. **Do Credit Counseling Agencies offer any other services to assist individuals?**
Nonprofit Credit Counseling Agencies provide financial education program and materials to their clients and, if they are genuine, to the general public. Many of these programs are free and available via the Internet. Others, such as seminars, may charge a reasonable fee.

13. **If I participate in a DMP, can I still get a mortgage, car loan, or credit cards while on program?**
While policies governing such loans vary from lender to lender, it is still possible to qualify for a mortgage while on a Debt Management Program. The same can be said of car loans. However, a letter from the Credit Counseling Agency stating that you have made a certain number of on-time monthly payments is often required by the new lender. It should be the individual's and the Credit Counseling Agency's goal to avoid ALL credit card and other unsecured debts while on the DMP. Consequently, the individual is unlikely to qualify for credit cards while on the DMP.

What is Debt Settlement?

Simply put, debt settlement is the process of negotiating with a creditor to reduce the amount of the debt owed. Individuals can often negotiate such a reduction of debt on their own, thus avoiding the fees of companies that offer to do so for them. Individuals considering such a process should keep in mind the many drawbacks, including:

- Settling debts will trigger a negative mark that stays on their credit for at least 7 years.
- Never give money to a debt settlement company without investigating their history (see www.BBB.org, for example) and getting a written contract.
- There is certainly no guarantee that a creditor will accept the terms of the settlement, whether you are proposing them to the creditor yourself or paying someone else (including an attorney) to do so for you.
- If a settlement is reached, the amount of debt forgiven by the creditor is very often taxable. Debt settlement companies also tend to base their fees on the amount of debt forgiven. So, as an example, even if a settlement company achieves a 50% reduction of a $10,000 debt that you owe, you can often expect to pay the settlement company a $1,250 fee and possibly owe another $1,000 to $2,000 to the IRS. That means that you end up paying $7,000-$8,000 on the original $10,000 debt AND your credit damaged for at least seven years.

What is Bankruptcy?

Bankruptcy is a legal petition filed in a federal court. Bankruptcy law serves two general purposes: first, to protect certain assets of an individual or household from creditors while canceling many debts in order to provide a fresh start to the consumer, and second, to provide the creditor some recourse for payments (partial or full) on the debts they are attempting to collect.

Filing for bankruptcy will negatively affect an individual's credit for at least seven years and will stay on their credit reports for ten years. Also, there are many non-financial circumstances, including certain job applications, that may ask whether or not the individual has EVER filed for bankruptcy. In such cases, the 10-year time limit does not apply.

3. Financial Danger Zone

Easy Credit, Lasting Pain

How Payday, Title, Pawn, and Other Expensive Loans Work

When we regularly spend more then we earn, we go deeper and deeper into debt. As consumers, we often look for "quick-fix" solutions to our debt and for ways to continue surviving from paycheck to paycheck. Often, however, what starts out as a seemingly innocent idea quickly deteriorates into severe financial problems. Following are examples of such "quick-fix" solutions

Payday Loans

Although illegal in some states, payday loan and check cashing companies are popular options for obtaining small loans across most of the United States. These businesses have surfaced in strip malls, shopping centers and even gas stations. They come, however, with a hefty price because of the fees charged. The annualized interest rates of these loans can range from 340% to over 1000%, depending upon the company you choose, how much cash you want to borrow, and how long you take to repay the loan. Loans are repaid with one lump sum at the end of the term. Payday lenders often take the payment directly and automatically out of the borrower's checking account. Furthermore, some reports indicate that the average first-time payday loan borrower will have taken out EIGHT payday loans within a year!

Title Loans

These short-term (often 30-day) loans are typically tied to a vehicle that, if the loan is not repaid as agreed, can be repossessed and sold. Typical interest rates range from 100% to 200% or more. Loans generally do not exceed 50% of the value of the vehicle and are repaid with one lump sum at the end of the term. Otherwise, the lender (who usually collects a key to the car at the front end of the loan) may repossess the vehicle. Borrowers need to be aware of additional "hidden" fees that some lenders try to charge. In states where title loans are explicitly illegal, they may still exist under names like, "Sales and Leasebacks" or "Car Pawns."

Rent-to-Own

Establishments that offer furniture, appliances, and A/V equipment on a rent-to-own basis often end up charging total payments that work out to be 100% to 700% of the actual retail cost. That means that if the consumer were to be patient for one year, putting those same payments in their savings, they could purchase two to seven equivalent items plus have earned some interest in the bank. Consumers should also keep in mind that the payments advertised by these establishments are usually weekly payments, not the typical monthly payment of other loans. Moreover, if just one weekly payment is missed, the store may take back the item and the consumer will lose the value of all previously-made payments.

Tax Refund Anticipation Loan

Some tax filing businesses will offer what is called a "Tax RAL," (Refund Anticipation Loan). They offer their customers the opportunity to walk out that same day with 50% of their refund as a loan, with the remaining balance available the very next day. Unfortunately, the remaining balance does not equal 50% of the anticipated refund. Instead, the business charges a hefty fee that can equal an annualized interest rate of 40% all the way to 700%! Tax payers should instead consider the value of being patient and having their refunds deposited directly into their checking accounts within two weeks.

Pawn Loans

Getting a loan through a pawn shop will usually mean that you're paying an annualized interest rate of around 100%. These loans are typically for a short period, often just 30 days. Loans of around $70-100 are usually made on household items, though they can be for as little as $20 or as much as several thousand dollars, depending upon what is being pawned.

It is often the case that once an individual begins depending upon such short term and expense loans, they become stuck in a vicious financial downward spiral. Unable to pay the original loan amount and the fee when they are due, the individual may unwisely find another similar loan elsewhere to borrow even more money in order to repay the original loan. In a matter of just a few months, the fees alone can be equal to or greater than the original amount of money borrowed.

While these loans are already difficult to justify, they too often result from poor money management or from poor judgment in frivolous expenses such as frequent dining out, expensive entertainment, and new consumer goods.

4. Resources

Internet Resources

- ABA Education Foundation: www.aba.com/ABAEF
- American Savings Education Council: www.ChooseToSave.org
- Bankrate: www.BankRate.com
- Bankruptcy Basics (US Bankruptcy Court): www.uscourts.gov/bankruptcycourts/bankruptcybasics.html
- Better Business Bureau (Scam & Fraud under "Alerts"): www.bbb.org
- Choice Nerd: www.ChoiceNerd.com
- Citi Financial Education: http://curriculum.FinancialEducation.citigroup.com
- CNN Money: http://money.cnn.com/pf
- Community Action Partnership: www.ManagingMyMoney.com
- Consumer Jungle: www.ConsumerJungle.org
- Credit Abuse Resistance Education (US Bankruptcy Courts): www.careprogram.us
- Credit Bureaus
  - Equifax: www.Equifax.com
  - Experian: www.Experian.com
  - TransUnion: www.TransUnion.com
- Credit Union Personal Finance Tips: www.creditunion.coop
- Debt Reduction Services:
  - Blog: www.debtreductionservices.com/blog
  - Facebook: www.facebook.com/DebtReductionServices
  - Twitter: http://twitter.com/debt_helpers
  - YouTube: www.youtube.com/debtreductionvideos
  - Web: www.DebtReductionServices.org
  - Tel: (877) 688-3328
- Gamblers Anonymous: www.gamblersanonymous.org
- Emergency Financial First Aid Kit: www.OperationHope.org/effak
- Federal Reserve Education: www.FederalReserveEducation.org
- Federal Trade Commission: www.ftc.gov/bcp/menus/consumer/credit.shtm
- Financial Football: www.WhatsMyScore.org/games/ff
- Financial Fundamentals (JP Morgan Chase): http://bit.ly/ayo9XR
- Financial Life Planning Center (Key Bank): www.key.com/html/savings-resources-planning.html
- Financial Soccer: www.financialsoccer.com
- Financial Tools Center (Bank of America): http://learn.bankofamerica.com
- Freddie Mac: www.freddiemac.com/corporate/buyown/english/preparing/right_for_you
- Free Annual Credit Report: www.AnnualCreditReport.com
  - Tel: (877) 322-8228
- Hands On Banking/El future en tus manos: www.HandsOnBanking.org
- HIP Pocket Change: www.USMint.gov/kids

Internet Resources

- HUD's Hope for Homeowners: www.hud.gov/hopeforhomeowners
- Investing for Students: www.InvestingForStudents.org
- Jump$tart Coalition: www.JumpStart.org
- Kiplinger: www.kiplinger.com/money
- Liz Pulliam Weston: http://asklizweston.com
- Military Financial Education: www.pioneerservices.com/PioneerServices/finEducation.do
- Mind Your Money: http://bit.ly/c1pztI
- Money Savvy Generation: www.msgen.com
- Money Smart (FDIC): www.fdic.gov/consumers/consumer/moneysmart
- Money$marts for Girl Scouts: www.girlscouts.org/moneysmarts
- MoneyTrack PBS: www.MoneyTrack.org
- Motley Fool: Educate, Amuse, Enrich®: www.fool.com
- MSN Money Central: http://moneycentral.msn.com/personal-finance
- Council for Economic Education: www.councilforeconed.org
- National Endowment for Financial Education: www.nefe.org
- National Financial Education Center
  - Blog: day2daymoney.wordpress.com
  - Facebook: www.facebook.com/MoneyDay2Day
  - Twitter: twitter.com/MoneyDay2Day
  - Web: www.NationalFinancialEducationCenter.org
  - Tel: (877) 688-3328
- Native Financial Education Coalition: www.nfec.info
- Northwest Education Loan Association (College & Loans): www.nela.net
- Oprah's Debt Diet: www.oprah.com/subtopic/money/debt
- Planet Orange: www.orangekids.com
- Practical Money Skills for Life: www.PracticalMoneySkills.com
- Social Security Retirement Benefits Estimator: www.socialsecurity.gov/estimator
- The Mint: www.TheMint.org
- US Financial Literacy and Education Commission: http://MyMoney.gov
- What's My Score: www.WhatsMyScore.org
- Yahoo! Finance: http://finance.yahoo.com/personal-finance
- Your Financial Organizer: www.tiaa-cref.org/pubs/html/financial_organizer

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