



Reducing Debt

If your goal is to reduce your debt load, here are some helpful hints to plan your strategy.

Prioritize your debts

Mortgages or other secured loans, such as auto loans, should take first priority. If you default on these kinds of loans, you can face foreclosure or repossession. If, for example, your car is repossessed, it may affect your ability to work and adversely affect your income. Additionally, the car will be sold or auctioned off. If the sale of the car brings in less than you owe, you still have to pay the difference! In effect, you could be sitting on the bus and still making car payments.

Use cash for new purchases

Unless you pay off the entire balance every month, you are probably paying interest on new purchases from the date of the purchase. If you stop using your credit cards all together, you will be able to reduce your debt more quickly. Because of compounded daily interest, it is far better to use cash for the things you need and adjust your budget to accommodate those expenses than to use credit cards and then struggle to send large payments.

Set your own payment

Establish a budget and a tracking system for your income and expenses. Then you will know how much money you have available for credit payments. This amount must be more than the creditor's minimum payment. Once you have established amounts for each creditor, send your payments in regularly. When smaller balances are paid off, apply that money toward increasing the payments to your other creditors.

Pay more than the minimum amount due

When you compare the finance charge column and the minimum payment column, you might see that most of your payment is going toward interest and little goes toward the principle. When you increase your payment, the additional funds are applied directly toward the principle. Years of payments and thousands of dollars can be cut from the life of a debt simply by adding a few dollars to the payment. For example, if your minimum payment is \$25 and \$19 dollars are going to pay interest, then that leaves only \$6 for the principle. If you increase your payment to \$31 this month, it is like making two months payments toward the principle-essentially doubling your payment. The more you increase your payment, the less you will ultimately have to pay.

Pay off higher interest rate cards first

Dedicate more money toward higher interest rate cards because you will ultimately save in interest. It is better to owe \$100 on an account that has an APR of 14% than to owe \$50 to one at 14% and \$50 to another at 19%. Note if there are cash advances on any accounts. Cash advances usually command higher interest rates than balances on purchases. Usually, your creditor will divide the payment on a percentage basis between the two balances. If you increase your payment, the creditor will divide additional payments along the same guidelines unless you specify otherwise. For accounts such as this,

after you decide how much extra you can send, consider making the minimum payment as usual and write a separate check for the extra funds. Stipulate in writing that the extra payment is to be applied directly to the principle balance for cash advances. Verify how the payments were distributed in your future statements.

Pay your bills when you receive them, not when they are due

Most creditors use the Average Daily Balance method of calculating interest. Reducing the average daily balance by making your payment sooner will ultimately reduce the amount of interest you pay.

Don't accept your creditor's offers to skip payments

Interest continues to compound while you're skipping your payment. The longer your balance goes without a reduction, the more interest you'll pay. If you've established your budget and have scheduled payments, continue to make those payments until the balance is paid off.

Consider transferring balances to lower rate cards

You may receive offers of credit with low-interest teaser rates. These low rates are called teaser rates because they usually only last for 3 to 9 months. They offer to transfer balances from your other credit cards to theirs with the lower interest rates. In general, an opportunity to pay less interest is a fairly good idea but, if you are considering this step, you must consider more than the teaser interest rate. Examine the contract carefully before you apply for the card.