

Getting Out of Debt

A STEP-BY-STEP GUIDE





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Do you have
debt problems?

Credit card debt and other consumer debt are such a common part of modern life that many of us live with pressure on our budgets without realizing we may be entering a financial danger zone.

Are you one of the millions who are digging themselves into money trouble through the use of consumer credit? Are you trying to recover from a financial setback—a loss of income or an unexpected expense—that leaves you looking at a scary financial future? Are you getting by from month to month by building your debt instead of your savings?

Take this quick debt quiz to find out if you can use some help dealing with debt.

- YES NO I'm looking at different options for repaying my debt.
- YES NO I have debt to repay, but I'm also trying to decide how much money to put into savings.
- YES NO I carry credit card balances for a long time and often pay only the minimum amount due.
- YES NO My credit card balances are growing each month.
- YES NO I am at or near my borrowing limit on one or more of my credit cards.
- YES NO I no longer have a savings account, or I am using savings to pay bills I used to pay from my checking account.
- YES NO I try to manage my money to a budget, but I often come up short when I sit down to pay bills.
- YES NO I use cash advances from credit cards or the overdraft feature on my checking account to pay bills and basic living expenses.
- YES NO I borrowed from friends or family when money was tight and haven't yet paid it all back.

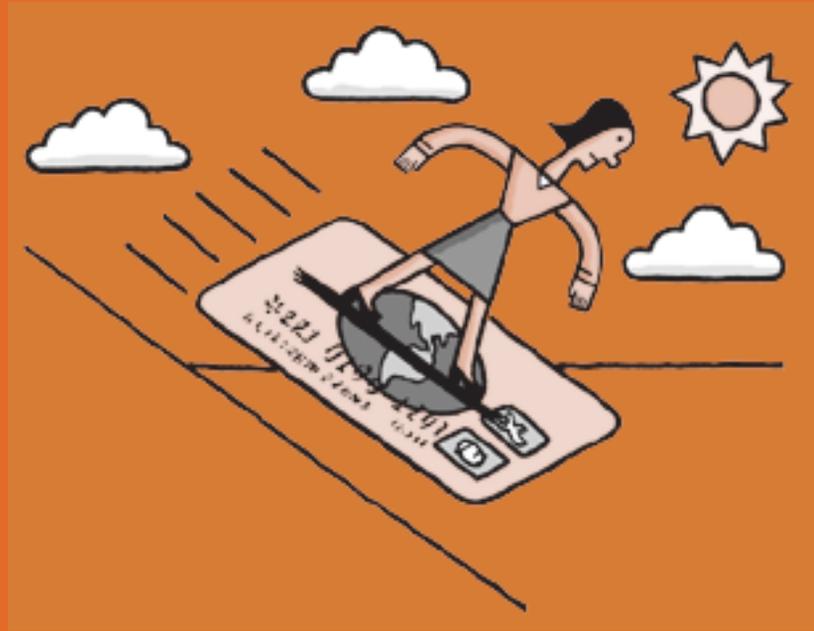
- YES NO I juggle payments, paying one creditor one month and another the next so that they are both getting something.
- YES NO I often transfer balances from one credit card to another because I can't afford to pay all of my monthly credit card bills.
- YES NO I have "consolidated" my debts into a home equity loan or a single credit card more than once.
- YES NO I rely on overtime pay or money from a second job to pay my regular bills.
- YES NO I don't have the money to pay irregular bills, like real estate taxes and insurance.
- YES NO When I come home from shopping, I sometimes hide my purchases or lie about how much they cost.
- YES NO I no longer pay attention to how much I owe.
- YES NO I sometimes get notices in the mail or phone calls telling me I'm late with a payment.
- YES NO My heart rate increases when my credit card is run through the machine because I never know if it will be accepted.

If you answered “Yes” to one or more of these questions, this booklet was written for you. Here’s what it will give you:

- The next section will tell you why it’s so easy to get into debt. Reading it should give you some insight into your own behavior. And the more you understand about why you’ve gotten into debt, the better you’ll do at changing the way you act with your money and reducing your debt.
- “Four steps to reduce your debt,” on page 13, gives you a step-by-step plan to change your spending picture and pay down your debts. This is the heart of the booklet.
- “Ask for help,” on page 34, explains how to find low-cost or free debt counseling services and support groups.
- “If you’re behind in your payments,” on page 38, “What about bankruptcy?” on page 42, and “What you should know about your credit record,” on page 47, give more specific information on issues of collections, bankruptcy, and credit reports.
- “Making your money work for you,” on page 52, shows how you can move from sinking in debt to building equity and begin to lay the foundation for a more secure financial future.
- Finally, “For more information,” on page 56, lists additional resources you may find helpful as you start on your path out of debt.

A word of caution

Getting out of debt takes time, commitment, and sacrifice. While this booklet is written to be quick and easy to read, some of the steps it offers will take work and perseverance. The emotional strain of living with a debt problem can be intense. But the road to financial security involves some emotional challenges, too. You’ll need to decide that the pressure you face from your debt is worth the self-discipline it will take to retire it and get back on firm financial ground.



Why it's so easy
to get into
debt trouble

Americans owe more than \$2.3 trillion in consumer debt, more than 15 times what they owed in 1970.

FEDERAL RESERVE BOARD

Let's start with the positive aspects of debt. After all, there are reasons that banks offer credit cards and people take on debt. Then we can look at the problems that debt can create.

The benefits of debt and credit

When you and millions of others buy with credit, you're fueling our economy by increasing the demand for goods and services. Your spending creates work, jobs, and wealth for the people who provide those goods and services—and it brings money in interest payments to banks and other lenders. The money from your spending encourages innovation and invention as people look for ways to design better products and new, more efficient ways to deliver services to sell to you. And that growth and innovation is what moves all of us, over time, to a higher standard of living.

That's the big-picture benefit of debt and credit. At the individual level—yours—credit has immediate benefits, too. Used carefully, it allows you to buy what you need now and pay for it out of your future earnings. Credit in the form of home mortgages is the lever that allows ordinary people to own their own homes and gradually build a valuable investment for their future. Student loans allow people who couldn't otherwise afford it to attend school and learn skills that increase their earning power.

Why it's so easy to get credit

Until the early 1970s, credit was available to most people only for significant purchases—a home, car, or big piece of furniture—where the lender had something valuable to recover if the borrower fell behind in the payments. Lenders were cautious about loans and made sure they had an easy way to recover the money if anything went wrong. For most purchases, people saved until they had enough to pay cash.

That changed with the introduction of credit cards in the 1970s. Lenders discovered a huge and profitable new market of borrowers. And we, the credit card spenders and borrowers, discovered the convenience of cash-free spending and the pleasure of getting what we wanted without waiting until we had the cash to pay for it.

The average credit card holder has 8.7 credit cards and owes about \$8,000 in outstanding credit card debt.

STATISTICAL ABSTRACT OF THE UNITED STATES

Which leads us to where we are today. We live in an age of easy credit. And that requires a new kind of financial discipline and self-control. Credit makes it easy for us to get what we want. But it also makes it easy to get into serious financial trouble.

Why it's so easy to get into debt trouble

Credit cards are a great convenience. They let us buy what we need even when we don't have enough cash. They make it easy for us to shop online, buy meals, and rent cars when we travel. But credit cards also tempt us to spend more than we can afford.

Studies of consumer behavior show that people spend two to three times as much money when shopping with a credit card as they do when paying with cash. The difference is in the level of impulse shopping. The act of paying with cash reminds us that we have a limited amount of money. We tend to forget that limit—or ignore it—when we pay with a credit card.

When relying on cash, people are more likely to be disciplined in their buying and do a better job of ignoring the many impulse temptations they face. Because the cash is hard to part with, they tend to take extra time to find the best bargains. When paying with a credit card, shoppers tend to be much freer with their spending. They pick up those tempting extra items and add them to their carts. They also spend less time comparing prices and looking for bargains.

It goes even further. Credit cards free us to be more generous when shopping for gifts. They make us looser with our money when choosing food and drinks in a restaurant, and when leaving tips. And when we know we'll be paying with plastic, it's harder to buy just the one inexpensive item we were looking for. We add a couple of other things to the cart so we don't look silly charging a small amount when we get to the front of the checkout line.

The personal savings rate (the percentage of annual income that the average American puts into savings) dropped from 8.4 percent in 1980 to 5.2 percent in 1990. In 2000, for the first time, the savings rate was a negative number. Americans, on average, spent more than they earned.

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The many ways to borrow

Debt isn't limited to credit card spending. We give credit cards extra attention in this booklet because they offer such an easy way to get into debt. But there are other ways of spending beyond your means. Here are a few:

- Loans from parents and other family members
- Money borrowed from friends or co-workers to cover lunch or small expenses
- Gas station cards
- Store account cards
- Paying late, or over time, for services such as dental work and car repairs
- Stretching your budget by paying regular monthly bills late (in effect, borrowing from the companies to which you owe money)
- Payday loans (loans to cover expenses just before payday—generally at very high interest rates)
- Advances on wages or commissions from your employer
- Borrowing from a life insurance policy
- Credit reserve or overdraft privileges on a bank checking account

These are all ways to pay for things before you have the money to cover the expense. And they're all ways to accumulate debt.

The emotional side of spending and saving

We all know, at least at some level, that we should have enough savings to weather a financial setback—the loss of a job, an injury or illness that interrupts or reduces income, or a costly expense. We know that we should be steadily building up our savings—for retirement, our children's education, or for the down payment on a home. We know that increasing our savings and reducing our debt over time is good for us. Yet for the population as a whole, the rate of savings is shrinking and the level of personal debt is rising.

The average college senior carries
6.2 credit cards with total debt
of more than \$3,000.

Nellie Mae

Why do we often act in irrational and self-destructive ways with our money? A big part of the answer is that we aren't calculating machines. We aren't very rational. We're human beings with complex emotional needs. And access to money and credit plays to our emotions in ways that are hard to control.

At a primary level, there's the tension between "now" and "later." Spending brings immediate pleasure. We don't enjoy the benefits of saving—or the pain of debt payments—until later. We may think of ourselves as mature adults, but there's still a lot of the two-year-old in each of us. "I want it now" can easily overpower "But think about later."

The way we behave with our money is also deeply rooted in our experiences, especially in childhood. For example, if you grew up with a parent who was a disciplined saver and never spent money on fun extras, you may find it easy to follow that model yourself. Or you may find yourself behaving in ways that are a reaction against that early experience. At a level you may not even be aware of, you may view savings as an unhealthy form of self-denial and spending as a way to achieve a more balanced and happy life.

If you grew up in a household where there was never enough money, you may find yourself driven to make money, even at the expense of your own or your family's happiness, or to spend beyond your means in very visible ways. Early experience with money might be driving you to be overly cautious with your money, or to take unreasonable risks.

Behavior patterns with money are also set early in life and can be hard to change. Older people, who established their spending and savings habits before the introduction of credit cards, tend to use credit cards as a convenience and not as a way to borrow. People who started their careers before 1970 are far more likely to pay off their credit card balances each month than are people who entered the work world after 1975. People old enough to have experienced the financial trauma of the Depression tend to be very cautious when it comes to debt and savings and very aware of maintaining a cushion against a possible money setback. And people who entered the work world during the boom of the mid- to late 1990s are more likely to have a freer and more optimistic outlook on their finances than people who have had trouble finding a job during an economic recession.

If you have a \$4,000 balance on a credit card that charges 18 percent interest and you make the minimum payment on time each month, it will take you 45 years to pay off the balance. By the time you do, you will have paid almost \$12,000 in interest in addition to the \$4,000 balance. That's if you're never late with a payment and are never charged a late-payment fee.

A good way to get a better understanding of your relationship with money is to talk about it with a trusted friend. Share stories of ways you've acted with money and talk about experiences you had with money growing up. If you're like most people, you'll find a connection between the two. The more you understand about why you act the way you do with your money, the better you'll do at noticing and dealing with things you do that may hurt your financial health.

The down side of debt

If debt is part of the engine that drives our economy and if it's such a wonderful convenience, what's the matter with being in debt? What's the down side?

The "snowball effect" of debt

Part of the problem is obvious. You build debt because you don't have the money on hand to pay for a particular item, and the debt then adds to your expenses for months and years to come. That makes it more likely that you'll need to borrow even more to pay your expenses in the future. Paying with debt solves the immediate problem, but it creates a bigger problem down the road. Once the debt cycle gets rolling, it takes real effort to turn it around.

The cost of interest

The second problem with debt is that it's expensive. It would be hard enough to pay back growing debts if you just had to pay the amount you borrowed. But you actually pay much more than that when you add in interest and late-payment fees.

Let's look at a typical credit card that charges 18 percent interest and imagine that you have an unpaid balance of \$1,000. If you make the minimum required payment of 2 percent each month, that comes to \$20. That seems reasonable and manageable.

If you pay \$20 the first month, you might expect your balance to go down to \$980. Then to \$960 the second month. At that rate, you'd pay the balance off in just over four years. But it doesn't work that way. This kind of calculation ignores the effect of interest.

Actually, your account is charged 1-1/2 percent interest each month (18 percent divided by 12). That comes to \$15 the first month. So you pay \$20, the bank adds \$15 in interest, and the balance drops by just \$5—to \$95. Instead of taking four years to pay off the balance, it will actually take eight years. And instead of paying back \$1,000, you'll actually pay back \$2,000. That's if you're on time with every payment and aren't charged any late fees.

If you're making just the minimum payment on a credit card that charges 18 percent interest, you're actually paying twice the price on the label or the receipt every time you buy with that card. So a \$60 pair of shoes will actually cost you \$120. A \$50 meal will actually cost you \$100. Try doubling the total next time you pay for something with a credit card and see if it seems like a good value.

The emotional cost of debt

The third cost of debt has to do with your emotional well-being. When your debt total is going up instead of down it can leave you feeling trapped, desperate, and not in control of your life. You can feel that someone else “owns” you, to the point that you deny yourself the breaks and pleasures you need to stay healthy and happy. A debt problem can drain your sense of confidence and self-worth. It can lead to depression, unhealthy anxiety, and health problems. The emotional effects can damage your marriage and your relationship with your children, friends, and extended family. Money problems are the single biggest factor in relationship problems that end in divorce. Debt problems can affect your performance at work, pushing you to overwork in a “nose-to-the-grindstone” way, and keeping you from contributing with energy and creativity in ways that add value to your employer and lead to bonuses, raises, and promotions.

Debt is clearly a two-edged sword. Used wisely and carefully, it can help bring you greater happiness and prosperity. Used casually and without careful planning, it can lead to economic crisis and intense emotional stress.

Symptoms of debt-related stress

- trouble sleeping
- loss of appetite or compulsive eating
- weight loss or weight gain
- headaches
- neck, shoulder, and back pain
- anxiety attacks
- frequent colds and other illnesses
- irritability and a quickness to anger
- withdrawal from social contacts with friends and family



Four steps to reduce your debt

If you've read this far, you're already beginning to take action to deal with your debt—just by thinking about it. Now it's time to really do something to get your debt under control. It takes just four steps. The first two are quick. They're just matters of commitment. The next two will take some time.



Admit that you have a problem and commit yourself to fixing it.

Only you can solve your debt problem. And you can only solve it if you decide that it's a problem worth solving.

There are a few ways of making that commitment. Some experts recommend writing a statement owning up to the problem and signing it. Others suggest that you call a family meeting and have an open discussion of the debts you face. A debt problem is rarely felt or solved by just one person, and the ideas and efforts of every member of the family may be needed to get you back in the black. People often find that this open acknowledgment of a debt problem is a relief to the others in their families. And it usually comes as no surprise.

The other effective way to make a commitment to solving a debt problem is to talk with a financial counselor or attend a meeting of others with debt problems. (You'll find some ways to make these connections in the next section, "Ask for help," which begins on page 34.) Talking about a problem pushes you to admit to yourself that you really do need to take action. Knowing that you'll be expected to talk again to that same person or group and report on your progress is also a powerful incentive to act—and to stay on track once you start. And finding other people who understand your problem and who have come up with ways to deal with similar problems can be a huge relief if you've been shouldering this worry yourself for a long time.

“There was a period of time when things really fell apart, when I didn’t know where I was at in terms of my finances. I didn’t want to balance my checkbook. I was afraid to.”



Stop debt spending.

Take your credit cards, store cards, and gas cards out of your wallet or pocketbook and put them in a secure, out-of-sight location at home. Starting right now, get through an entire day without borrowing money or charging anything. Pay cash, write checks, or use a debit or ATM card.

You’ll find that this in itself cuts your spending and pushes you to make only planned purchases. It will also show you what life feels like without debt spending. Most people are surprised at how easy it is to make the switch. Even travel and car rentals can be managed with cash and checks. A bank debit (or ATM) card is an easy alternative. It can be used just like a credit card, but without the debt effect. The money comes right out of your bank account every time you use it.

Once you get through today, you can decide about the next day. And if you manage that, take on another day.

After a week or so of no-debt spending, you’ll be ready to make an even bigger commitment. Keeping credit cards in a drawer at home is like closing a gate on a problem and not locking it. If you have a real debt problem, you need to lock the gate. Cut up your credit cards. And cancel the credit reserve or overdraft feature on your checking account. This will feel like a drastic step—like slicing through your safety rope when climbing a steep cliff. But in fact it’s the access to credit that’s the biggest danger to you until you get your debt down to a healthy level. Later on, once your finances are back under control, you can decide to ask for a new copy of one of your cards.

What about emergencies? Before 1970, people got through every imaginable emergency without credit cards. Try to imagine an emergency where a credit card would really make a significant difference. It’s not a hurricane or a flood. It’s not a fire. You’d just get cash from the bank. The only emergency a credit card can help you through is the “emergency” of running out of money in your bank account.

What about renting a car? It’s a myth that you need a credit card to rent a car. A debit card works just as well. And most rental agencies are happy to rent a car if you have good identification (a driver’s license and one or two other forms of ID) and a cash deposit (generally in the range of \$75 to \$300). It’s a little more trouble than a swipe of a card, and it’s worth making sure of the details in advance, but people do it all the time.



Make a spending plan.

A “no debt spending” policy will push you to pay more attention to your spending. The next step is to get a clear picture of that spending and develop a new spending plan.

You might think you already know how you spend your money. You know what your rent or mortgage is. You have a good idea of how much you spend on groceries. You may know how much you spend on transportation or gas. But without tracking your spending, you’ll find you don’t really know where all of your money is going.

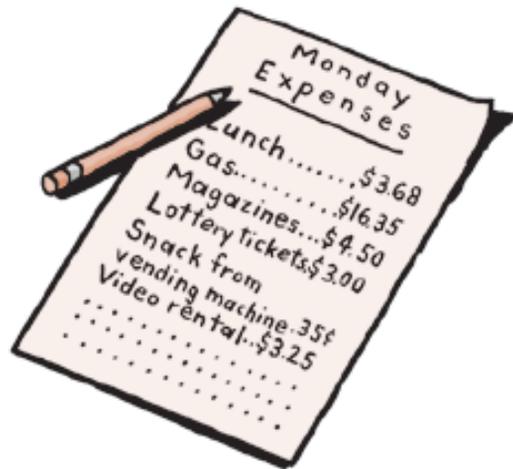
If you doubt this, take out a piece of paper and write down how much you made last year. Then total up those big categories of expenses you can track in your head. When you compare what you made to what you spent—at least in this quick measure—you’ll probably find that you should have ended the year with extra cash to put into a savings account. How does that compare with what really happened?

The reason it’s such a valuable exercise to track spending is that we have too many expenses to keep track of in our heads. And it’s the daily cash spending and the extra expenses—like car repairs, meals out, or holiday gifts—that push us into debt spending.

“When I was not managing my finances, thinking about it constantly was probably the worst. You obsess on it, and at the same time it’s almost as if you’re paralyzed. Now I don’t think about it. I just sit down with the credit cards and the bills twice a month. With a cup of coffee on a Saturday morning and it’s done.”

Track your cash spending

At the back of this booklet, you’ll find a set of tear-out slips for tracking your cash spending. Tear out the slip for today (or for tomorrow, if it’s late in the day and you want to start with a full day’s spending) and put it in your wallet with your cash. For one day, use the slip to write down every bit of cash you spend and what you bought with it—just like you use the register in your checkbook to make a note of the checks you write. Keep it simple so this doesn’t become a burden. All you really need to write down is the amount spent and what you spent it on. Like this:



Try it for a day. You’ll be amazed at how easy it is and how much it shows you. It takes just a minute or two to make the notes over the course of the day, and for that small effort you’ll find out just where your money is going. You won’t wonder any more what happened to that \$50 or \$100 you put in your wallet. You’ll know.

Once you see how easy it is, keep going. Track your cash spending every day for a week.

Here are a few ground rules to make sure you get the full benefit of the exercise:

- *Track your spending every day* (not just on the days you remember to do it). If you skip a day, you'll have a hole in your knowledge, a hole that could lead you to miss an important drain on your cash. If you find this hard to do, move your cash into an envelope and make your notes on the outside of the envelope. For some people, this is a better memory trigger.
- *Track every cash expense*, whether it's for \$25 or 25¢. If you skip some because they seem too small or because they're not part of your regular routine, you won't have a clear picture of your spending. You'll still be trying to manage your money in a fog.
- *Make your notes as you spend the money*. Keep a pen or pencil with you or borrow the store clerk's to make your note. If you wait and try to make your notes at the end of the day, you'll forget some. You'll still be operating in a fog.
- *Track spending to the penny*. Small change matters over the course of a week or a month.

Track the checks you write and payments you make with debit or ATM cards

Paying by check or debit card is the other main way people part with their money. If you're in the habit of recording every check you write and every payment you make with your debit card, that's good. If you're not in that habit, now is the time to start. Every time you write a check, write down the number of the check (so you can be sure you haven't missed any), the date, to whom you wrote the check, what it was for, and the exact amount of the check (to the penny). Every time you pay with your debit or ATM card, write the amount in your checkbook register just as you would with a check.

With this information in your checkbook register and the notes you're making on your cash spending, you'll be able to build a complete picture of your spending over time.

“The safest way to double your money is to fold it over once and put it in your pocket.”

KIN HUBBARD, IN “ABE MARTIN” SYNDICATED CARTOON

What about spending by credit card or charge card? Should you be tracking that, too? No, for two reasons. The first, and most important, is that you aren't using those cards right now. For today, you're not adding to your debt. The second is an accounting reason. You'll make payments on those cards to pay down the balance, and those payments will come from your checking account. What you're tracking here is the money as it leaves your checking account and the cash as it leaves your wallet.

Combine your notes into a weekly and monthly spending record

Once you have a few days of information on your spending activity, the next step is to start combining your numbers into a weekly and monthly spending record. A monthly record is the most useful measure, since so many expenses fall into a monthly cycle. A simple way to track spending by week so that you can total it up by month is to divide your weeks according to the days of the month.

- Week 1 starts on the 1st of the month and ends on the 7th
- Week 2 starts on the 8th of the month and ends on the 14th
- Week 3 starts on the 15th of the month and ends on the 21st
- Week 4 starts on the 22nd and ends on the last day of the month (so it will usually be a nine- or ten-day “week”)

When you track spending this way, your “weeks” will sometimes start and end in the middle of a week, and the fourth week won't be a true week at all. But four “weeks” tracked in this way will make a full month, and will include all of your monthly housing and utility expenses.

You can use the form on the next page for this tracking. Feel free to change the categories or add categories to make it easier to group your expenses. Just don't make it too complicated. The idea is to get a clear picture of your expenses, not a microscopic image of every detail.

Monthly Spending

WEEK 1

WEEK 2

WEEK 3

WEEK 4

TOTAL FOR
MONTH

SPENDING
PLAN

Month of _____

	WEEK 1	WEEK 2	WEEK 3	WEEK 4	TOTAL FOR MONTH	SPENDING PLAN
Mortgage or rent						
2nd mortgage/equity loan						
Property tax/association fees						
Home maintenance						
Heat/fuel						
Electricity						
Telephone - basic						
Telephone - long distance						
Cellular/pager/Internet						
Water/sewage						
Trash						
Groceries/household goods						
Meals out/lunches						
Child care						
Child support						
Vehicle payment/lease						
Gasoline/tolls/parking						
Car maintenance						
Car insurance						
Public transportation						
Home owner's/renter's insurance						
Life insurance (outside of work)						
Medical expense (out of pocket)						
Dental/vision expense (out of pocket)						
Laundry/dry cleaning						
Clothing						
SUBTOTAL						

WEEK 1

WEEK 2

WEEK 3

WEEK 4

TOTAL FOR MONTH

SPENDING PLAN

TOTAL FROM PREVIOUS PAGE

- Cable/videos/DVDs
- Entertainment/hobbies
- Gaming (lottery, casino, etc.)
- Tobacco
- Alcohol
- Drugs/prescriptions
- Gifts/major/other
- Contributions/donations
- Health & beauty
- Pet/veterinarian
- License/dues
- Vacation/travel
- Lessons/tuition
- Kids' allowance
- Health club
- Emergency fund
- Other expenses

TOTAL EXPENSES

MONTHLY SAVINGS FROM MY SPENDING PLAN

Make a spending plan

If you're like most people with debt problems, you're in your current financial state simply because you've spent more than you earn. Now that you see how much you're spending (in the chart on the previous pages), you can make a plan to cut that spending to a level that will not only keep you from adding to your debt, but let you pay down your debt more quickly.

When most people begin to track their expenses, they find a couple of big surprises which then become the biggest opportunities for trimming their spending. It might be meals out. It might be books or movies. It might be car expenses. Whatever the surprises are for you, start there. The far right column of the chart, labeled "SPENDING PLAN," is where you should write down a realistic new goal for that category of spending.

In some cases, when people line up their expenses with their income, the expenses are so much higher than the income that drastic steps need to be taken. They may need to sell an expensive car and replace it with a less expensive model, or perhaps get rid of the car altogether and rely on carpools or public transportation. They may need to move to less expensive housing. This can happen when income is cut back, either through a change to a lower-paying job or a reduction in overtime pay. It can also happen when people move into a higher-paying job and overestimate how big an impact the change will have on take-home pay. If you're in this situation, it may help to talk with a debt counselor to get an expert opinion on what's pushing your budget so far out of balance. A good financial counselor can help you understand whether a drastic change is needed.

Almost always, though, it's not the home or the car, but the casual spending on meals out, music, movies, electronic equipment, and other "impulse" extras that have to be trimmed to make a healthier spending plan. And extra money can almost always be found through smarter shopping for the things now bought at too-high prices.

When the numbers just don't add up

For some people, a spending plan won't be enough to solve a debt problem. If your debts are from a severe financial upset—an expensive medical treatment, for example, or a permanent loss of earning power due to an injury or

disability—you may need more money than even the most rigorous spending plan will yield, and more help than this booklet can offer. Look ahead to the next section, "Ask for help," and get yourself the help and support you need.

“I have enough money to last me the rest of my life, unless I buy something.”

JACKIE MASON

The goal of a spending plan is actually very modest: to bring expenses into line with income, so that you stop adding to your debt, and to come up with an extra \$50 or \$100 a month to put toward debt repayment.

Here are some ways to trim spending that have worked for other people. Once you've looked them over, go back to the chart on the previous pages and find a few areas where you can realistically cut your spending—without trimming all the pleasure out of your life.

Entertainment

- Rent a video instead of going out to a movie or the theater.
- Borrow videos, music recordings, and books from your local library or from friends.
- Have potluck suppers instead of dinner parties.
- Go to museums, gallery exhibits, zoos, and aquariums at times when admission is free or reduced. Find out if your library offers free museum passes.
- Trade babysitting services with other parents or join a babysitting cooperative.

Eating out

- Eat out less often.
- When you do go out to eat, leave your credit card at home. Pay with cash.
- Look at the menu and the prices before you go into a restaurant. If there isn't a menu in the window, ask to see one before deciding whether to eat there.
- Don't order drinks with your meal. Stick to water. If you do order drinks, limit yourself to one per person.
- Don't order dessert. Order coffee if you want an extra ending to your meal.
- Bring leftovers or a sandwich to work for lunch.
- Make coffee at home and bring it in a thermos to work or to school.

“Beware of little expenses; a small leak will sink a great ship.”

BENJAMIN FRANKLIN

Food

- Read the newspaper and the advertising fliers that come to your home. Compare prices and look for bargains.
- Clip coupons and use them to buy the items and brands you use regularly. (Never use coupons to try a new item or to buy something you wouldn't have bought otherwise.)
- Shop from a list. Make the list from a weekly menu.
- Eat before you shop for groceries. You won't be as tempted to buy extras.
- Join a discount club (such as Price Club, Costco, or BJ's Wholesale Club) to get lower prices on such staples as paper goods, cereal, coffee, and peanut butter.
- Don't buy soft drinks, pastries, chips, or other junk food. A baked potato, chopped vegetables, a sandwich, or leftovers from dinner make healthier and cheaper snacks.
- Buy less prepared food, and prepare more food yourself.

Getting around

- Shop for the best price on car insurance. See if you qualify for insurance discounts (for a good driving record, AAA membership, or low mileage).
- Have repairs done by muffler, transmission, brake, and tire shops. These services often do work at about half the price of car dealerships.

Clothes

- Shop from a list and pay with cash. Bring only enough to buy what's on your list.
- Buy on sale—after Christmas, Easter, and the 4th of July, when seasonal clothes are discounted.
- Buy clothes in colors and styles that go together, so that they can be worn in many different combinations.
- Buy higher quality clothes at the best price you can find. Look for classic designs, solid construction, and materials that last.
- Buy washable clothes, not clothes that require dry cleaning.
- Trade clothes with friends or relatives as a way to expand your wardrobe.

“I’m very conservative with my grocery spending and we eat quite well. I watch for sales. We go to matinee movies. When we go out to eat, which is fairly rare, we go to places where the kids eat free.”

Household

- Cover drafty windows using a plastic storm-window kit. Lay a rolled-up towel or a special sand-filled fabric “log” along the bottom of any doors that let in cold air. Seal window and door frames with caulk.
- Keep window shades down to block out the sun in hot weather. Leave shades up to let in warming sunlight on cold sunny days.
- Write letters or send e-mail messages instead of making long-distance phone calls.
- Shop for the best price on telephone, cell phone, and Internet access plans. Consider dropping your cell phone service.
- Discontinue cable TV, or cut back on optional channels.
- If you have a weekly cleaning service, cut back to every other week or drop the service and do the cleaning yourself.
- Buy a neighborhood lawn mower, snow blower, hedge trimmer, or barbecue grill.

Health

- Walk, run, or bicycle outdoors. Healthy exercise can be free.

Extravagances

- Look at money you may be spending on an expensive hobby or high-priced lessons or programs for your children. Fun for you and enrichment and learning for your children don’t have to be expensive.
- Look at any money you may be spending on cigarettes, alcohol, drugs, or gambling. You may be able to take a big step in dealing with your debt by kicking an expensive and unhealthy habit.

Make an earning plan

For most people, the key to getting out of debt lies in more careful spending. But you may also have some opportunities to increase your income, which is the other way to come up with more money for debt repayment. Just be careful not to let your debts push you into a miserable grind of round-the-clock work. The goal is to get your debt down to a level where it no longer controls your life. You want to be in control of your money and your life.

Workaholism is not the answer. Finding ways to enjoy life while living within your means is ultimately the path that will lead you out of debt.

With that caution, there may be ways to turn your new focus on finances into extra money. You might

- Have a yard sale
- Sell a valuable item by advertising in the newspaper or offering it for sale through an online auction site
- Turn a hobby or a special skill into a money-making activity
- Collect any old debts that others owe to you
- Find a part-time job to supplement the income from your primary job
- Take in boarders or find a roommate
- Provide repair or chore services to older people in your community who need help

Jot down any ideas of your own in the space below. Refer back to your list and add to it as you try out your spending plan. You may find that some extra income helps you get your debts down even faster.

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Look back at your monthly spending chart on pages 20 and 21. Write down your new spending goals for every category of your spending. Some may not change at all and you may be able to cut others dramatically.

Now estimate how much you can save every month if you follow your plan. Add to that any extra money you think you can make. Write the amount down at the bottom of the chart.

This is what you'll be able to pay each month, starting now, toward reducing your debts and building an emergency savings account.

4

Pay down your debts month by month. Pay them off one by one.

The next step is to make a list, using the form on the next page, of all the debt payments you make each month. Include payments on credit cards, store cards, installment loans, home equity loans, payments to repay personal loans to friends and family—payments on everything you owe to anybody. (Don't include mortgage payments. Like rent, they are a basic housing cost. And unlike your other debts, you can pay off your mortgage at any time by selling your home.)

For each debt, list

- The name of the creditor (the bank, credit card, business, or person to whom you owe money).
- What you normally pay (what you'll pay this month if it varies).
- The total amount you owe (the exact amount from your most recent bill or statement).
- The annual interest rate that is applied to the balance. (If that interest is set at a special low rate for a limited time, write down the date that it will go up.)

The interest rate may be hard to find. It may be buried within the small type on the back of your bill. If you can't find it listed on your bill or statement, call the creditor and ask what interest rate is being charged on your account.

Many credit cards have different rates for balance transfers, purchases, and cash advances. Your bill should show how much of your balance falls into each of these categories, and what the interest rate is for each. If you have balances in more than one category, estimate or use a calculator to figure out what the average interest rate is for the entire balance on that card.

“Our main approach is, first and foremost, don’t make the debt bigger. We got credit cards that wouldn’t allow us to carry a monthly balance. And then we really tried to be disciplined about the past credit card debts we owed. And sure enough, over the course of the last three years we’ve paid it down quite a bit.”

Look back at your monthly spending chart and the amount you decided that your spending plan would save every month. Divide that savings amount in half. This is how much you can add to your debt payments, starting this month. (You’ll put the other half into a savings account as a cushion against any interruption in your income or unexpected expenses. We’ll discuss this in the last section. If you already have \$2,500 or more in a savings account, then you can apply the entire amount saved from your spending plan to reducing your debt.)

Monthly savings from my spending plan	My monthly debt payment allowance
\$ ÷ 2 =	\$

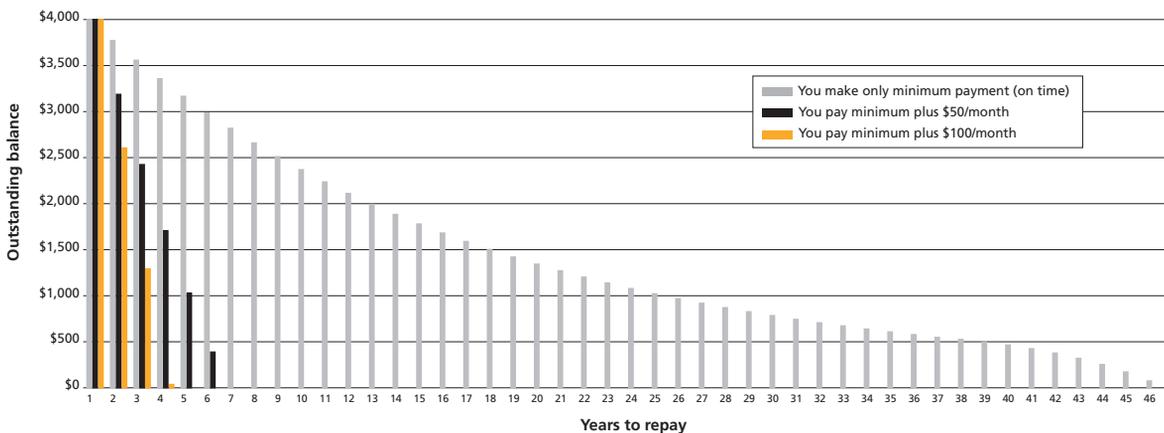
Now look at your list of debts. Choose one to pay off first. It should either be the one with the highest interest rate or the one with the lowest balance. It’s your choice. The one with the highest interest rate is costing you the most every month. You’ll make a bigger impact on your spending if you pay that one off first. But the satisfaction of paying a loan off completely is an important motivation, and that will happen sooner if you choose the loan with the smallest balance.

Starting this month, add your extra debt-payment allowance (the amount you calculated above) to your payment toward the debt you’ve singled out. So if you had been paying the minimum of \$20 a month on a credit card bill and you’ve decided you can add \$50 to your debt payments, you’ll pay \$70 a month toward this card. Keep making your regular monthly payments toward the other debts. You’ll get to them next.

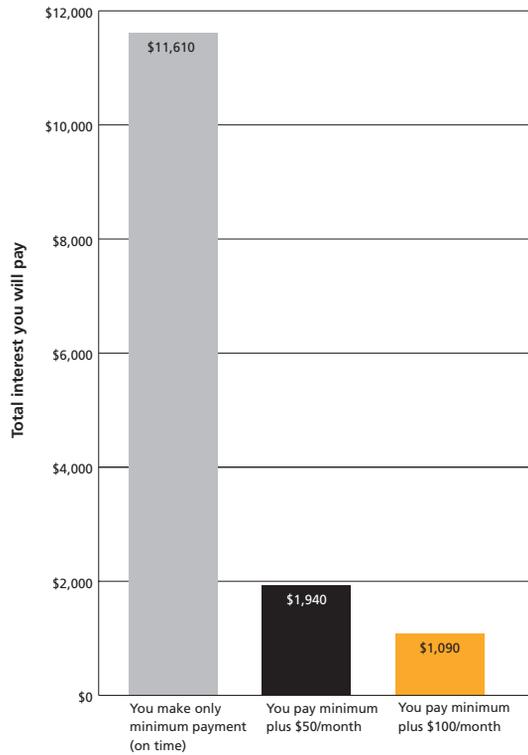
An extra \$50 or \$100 payment every month may not seem like much, but it makes a huge difference in how long it takes to repay a debt and to the total amount you pay. An extra \$50 per month can reduce the time it takes to pay off a \$4,000 credit card balance from 45 years to less than six years. And it can reduce the total amount of interest you pay from more than \$11,000 to less than \$2,000. Paying an extra \$100 per month reduces the payoff time to just over three years and the total interest to just over \$1,000.

As you focus your repayment efforts on that one debt, you'll have the satisfaction of seeing the balance shrink over the course of several months until it finally disappears. When that happens, it will be time to move on to the next debt. (As with the first one, you decide whether it's the loan with the smallest balance or the highest interest rate.) And here's where the magic of interest rates starts to work in your favor. When you pay off the first debt, you free up the money you were paying in interest on that loan. Now you'll be able to pay even more each month toward the second debt. And the speed of your repayment plan will begin to pick up.

Payoff rate for \$4,000 credit card balance



Interest on \$4,000 credit card debt



Let's say you were paying \$70 a month toward the first loan (the \$20 minimum payment plus the \$50 you added). And let's suppose the minimum payment on the second loan is \$30. You can actually afford to pay \$100 a month toward that second loan now (the \$70 you were paying toward the first loan, plus the \$30 minimum on the second). You just need to keep to your spending plan. You'll be paying the same amount of money toward your debts, and those debts will be disappearing faster.

Stick with it

This four-step plan is a sure-fire way to reduce your debts. It's a strategy that's worked for thousands of people who have overcome serious debt problems. It's the basis of the support offered through professional debt counseling and through groups such as Debtors Anonymous. But it's not a quick fix. It takes time. And it takes your steady commitment to stick with the plan.

You may be tempted to skip a month sometimes or to make an exception and charge something on a credit card or store account card. Nobody will stop you. It's your money, your debt, and your responsibility. But from your own math and the graphs in this booklet, you can see that any slips will set you back and delay the success of the plan. Just as debts can "snowball" and build up to get you in debt trouble, so a debt repayment plan can snowball in the opposite way, picking up speed and becoming easier as you shed more and more of your debt interest payments.

So stick with it. And watch as your debt steadily dwindles until it finally disappears.

What about consolidating debts?

If the goal is to have fewer loans and lower interest payments, doesn't it make sense to consolidate loans into one larger loan—by transferring balances to a lower-interest credit card or a home equity loan? The surprising answer is: probably not. It's true that you want to reduce your debt payments. They're a big drain on your budget. But the way to do this is by reducing your debt, not just by moving the money around.

If people acted like financial-planning machines, it certainly would make sense to consolidate loans. But people don't act like machines. When they consolidate loans, most people end up running their debts back up on their other credit cards. So they're left with the same credit card problems they had before—and now a large consolidated loan on top. Consolidating loans seems to encourage people to build up even bigger debts, rather than helping them reduce their debts.

The two main options for consolidating loans each have serious drawbacks. Many people respond to credit card marketing pitches that offer special low interest rates on

balance transfers. But the low rates are usually for a limited time—generally through the end of the year. After that, the rates go back up to levels that are often as high or higher than the rates on other cards. And while people usually intend to pay that card off before the rate goes up, they rarely do. Also, if they use the card for new purchases, in addition to the balance transfer, they find that the special rate doesn't really apply. A higher rate applies to new purchases, and payments go to pay down the low-rate balance first, which leaves a growing balance of high-interest debt on what was supposed to be a low-interest card.

Home equity loans really do offer lower interest rates. But there's a reason for that. A home equity loan is "secured" by the value of your home. If you fall behind in your payments, the lender can force the sale of your home to recover your debt. That's a serious proposition. A home equity loan is only a sensible option for people who already have their debt under control.



Ask for help

You may be able to work down your debts just by following the advice in this booklet. But it may be easier for you to stick with a plan if you have some regular one-on-one coaching time with a professional financial adviser or credit counselor. And you may have better success over the long term if you have a chance to talk with others who are facing similar problems.

An expert can help you translate the information and suggestions in this booklet and from other sources into a personalized plan that takes into account all of the factors that make your situation unique. An expert can tell you how serious your problem is, whether you've analyzed your numbers correctly, if there is other information you should be thinking about, whether it's worth trying to negotiate with your creditors to reduce your debt payments, and if there are other options for you to consider that haven't been mentioned in this booklet. And both a credit counselor and a support group can help you put your problems in perspective.

For some reason, it's considered rude in our society to talk about money. Most people are more comfortable talking about sex, death, or virtually any other painful or awkward topic. But by not talking about our money problems, we end up bearing the weight of our money worries alone. Statistics show that a huge number of people have money problems. A million and a half Americans file for personal bankruptcy every year. Roughly 7 million have trouble paying their bills on time. Many millions more—roughly half of all credit card holders—aren't able to pay off their credit card balances every month. Yet most of us feel alone with our problems. We think that we are the only ones who have debt problems. Worse, we feel that there is something wrong with us for being in the situation we're in—that debt is a sign that we're not good people, not successful, not worth much.

Being in debt has nothing to do with who you are. Sure, the stress and worry of a debt problem can affect how you act as a parent, a spouse or partner, a friend, or an employee or manager. But the debt itself has nothing to do with how well you do in each of those roles. You're the same person you were before you got into debt, with the same unique personality and the same strengths and skills. Part of the process of getting out of debt is getting back to feeling good about yourself—giving yourself permission to enjoy life and treat yourself well again.

That can be easier if you talk to people who understand the situation you're in—people who have been in the same difficulty themselves and worked their way out of it, or people who have successfully helped others deal with debt problems. That shared experience can help you understand that you aren't alone with your debt problem. It's your problem and you have to solve it. But you have plenty of company.

Talking with an expert or joining a support group has another key benefit. Regular meetings give you an incentive to stick with your plan. It's very easy to slip or to give up when you try to reduce your debt in isolation. It's harder when you know you have to check in next week or next month with someone else. The idea of admitting that you've made no progress is enough to motivate most people to keep on track.

Credit counseling options

- *Financial planners* help people save and invest for the future, but they can also help you with a debt problem. A financial planner may be a good option for you if you're carrying a high level of debt but also have significant assets, such as a retirement account, investments, or a large amount of equity in your home. When looking for a financial planner, look for someone who charges a fee for the consulting services (a “fee-only” financial planner) and doesn't charge commissions for any investments or transactions he or she recommends. And make sure you understand what that fee will be before you begin to work with a financial planner. Look, too, for a person with credentials to show the training and qualifications for the work. Look for a Certified Financial Planner (CFP) or a person with similar credentials. To find a financial planner, look in your local yellow pages telephone directory under “Financial Planning.”
- *Credit counselors* help people who are having trouble with credit card debt. The services of nonprofit credit counselors are generally free to low-income customers and very reasonably priced for others—in the range of \$25 per month. But be sure to ask about fees and find out whether the service is nonprofit before you begin working with a counselor. For-profit credit counseling services can be much more expensive.

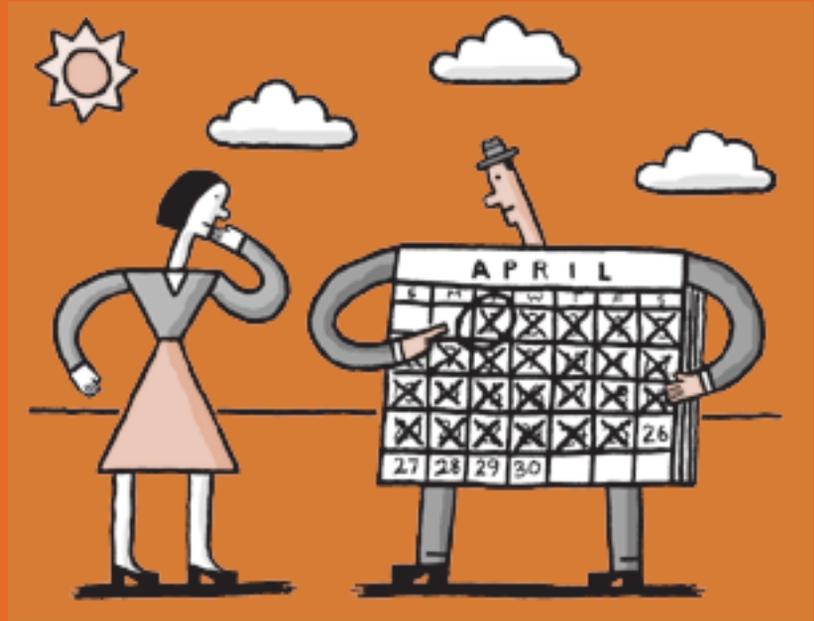
“It’s one of the worst feelings you can have, not knowing where the money’s going to come from. I didn’t know where to go, who to turn to. It’s just one of those things where you’ve got to ask for help and not be scared. I got some good advice and now I’m getting back on track.”

Credit counselors help their customers develop personal debt reduction plans. They can also step in as middlemen between you and your creditors to negotiate a repayment plan that you can afford. Credit counselors often take over the entire responsibility of working with your creditors. When this happens, you will be asked to make a monthly payment to the credit counseling service, and it in turn will make the payments to your creditors. You will be asked to sign a statement committing yourself to taking on no new debt. Depending on how serious your problem is, the credit counselor may also ask you to turn in and destroy all of your credit cards. To find a credit counseling service, look in your local yellow pages telephone directory under “Credit Counseling Services.” Look only for nonprofit services. For-profit services can be very expensive and are of uneven quality.

- *Your employer or union* may offer financial counseling at no charge to you. Check with your Human Resources department, a union representative, or the program that sent you this booklet to see if this service is available to you.

Support groups

Debtors Anonymous is a volunteer-run organization with chapters all over the country. Anyone can go to a meeting. There are no membership fees. And there’s no obligation to return if you find it’s not for you. At meetings, members help each other come to terms with and take responsibility for their debts. They also offer practical advice and strategies for repaying debts. Aside from the valuable practical information and advice that’s shared at meetings, Debtors Anonymous provides a social support network that helps people see that they aren’t alone with their debt problems. That social network, combined with a schedule of regular meetings, really does help people stay on track. See the resource guide at the back of this booklet for information on how to find a local chapter.



If you're behind
in your payments

If you've been getting notices or telephone calls about overdue payments, take the initiative to call those creditors. That may be a frightening prospect. If you're far enough behind in your payments that you've been getting collections calls, you probably want to avoid conversations with your creditors. When accounts get to the telephone collection stage, creditors tend not to be kind and soft-spoken. But you'll find that by making this call yourself, rather than waiting for the next collection call, you can transform a relationship where you are on the defensive into one where you and your creditor are working together to solve the problem.

When you call, tell your creditor that you've entered a program to get your debt under control, and that you'd like to work out a payment plan. As a start, ask for a 30-day moratorium on your payments. That will allow you time to pull your records together and come up with a plan for paying down all of your debts. If your credit hasn't already been shut down, suggest yourself that further borrowing be blocked. That gives another signal that you are serious about repaying the debt.

Creditors worry most about people who are ignoring their debts or who are actually being dishonest and trying to escape their obligations. By calling and telling the creditor that you're working on a debt repayment plan, you put yourself in the "good" camp of honest customers who are making a genuine effort to pay what they owe.

If you can't negotiate a 30-day break from the payments, find out what amount will satisfy the creditor. Pay that amount promptly. Your goal is to get back to a trusting relationship with the creditor, where the creditor knows you will honor your commitments.

Before the 30 days are up, and after you've had a chance to go through the rest of the steps in this booklet, call back and work out a repayment plan. At that point, you'll know how much you can pay every month without creating problems with other creditors.

Here are some guidelines for making these conversations productive:

- *Be honest.* Explain that you're trying to get your debt under control and be open about where you are in the process. If you haven't finished tracking your spending and adding up the numbers, tell the creditor that you've realized your budget is out of balance and you're doing the work now of coming up with a new spending and debt repayment plan.
- *Be prepared.* Have the information you'll need in front of you when you call. Make sure you know exactly how much you owe and when the payments are due. Be ready to offer a payment plan if you won't be able to pay the amount that's due by the date on the bill.
- *Put the conversation on an equal footing.* If a creditor calls you, don't get into a conversation right away. Politely ask them to hold on for a minute while you get out your records. When you get your copy of the bill and any notices you've been sent, get a paper and a pencil, too. When you get back on the phone, let the caller know that you're ready to talk now and that you'll be taking notes on the conversation. Start by asking them to give their name again and the name of the company they represent. Write the information down. Ask for the caller's telephone number and address and write that down, too. By doing this, you put the call on more of an equal footing. The caller knows who you are and has details of what you owe. Now you know who the caller is and you have the information at hand that you'll need to discuss a payment plan.
- *Be businesslike.* Remember that debts and their repayment are strictly business. A collection agent may try to make you anxious or put you on the defensive as a way to get you to agree to a payment plan. If you make it clear at the start of the conversation that you're ready to work out a reasonable payment plan—one that's acceptable to your creditor and within your means to follow—you can keep the conversation at a businesslike tone and keep it from becoming emotional. If the creditor yells on the phone or speaks in a rude or hostile manner, end the conversation and suggest trying another time when both of you can talk in a reasonable tone. If this happens more than once, ask to speak with the collector's manager and request another contact at the company.

- *Don't agree to more than you can manage.* If a creditor is pressuring you to pay more or repay a debt more quickly, you may be tempted to agree to higher payments than you can really afford as a way to get out of an uncomfortable conversation. Don't do it. You'll just fall behind again, and you'll have lost the trust of the creditor. It's far better to be honest and agree to pay only what you know you can afford.
- *Follow up with a letter.* If you and the creditor or collection agent agree to a repayment plan that includes reduced or missed payments while you get your finances back in order, follow up with a letter to confirm the agreement. An agreement like this usually includes the suspension of your credit privileges, so you may be sending your credit card with your letter as confirmation that you won't try to use it. Use a proper business letter format when you write. Keep one copy for yourself and send two to the creditor, asking them to sign and return one to you. Send your letter by certified mail, return receipt requested. When the signed receipt card comes back to you, keep it until you receive the signed copy of the agreement. Send a copy of the letter with each payment you make—and be sure to make those payments on time.



What about
bankruptcy?

Bankruptcy is the option of last resort for people with overwhelming debt problems. When you file for bankruptcy, you are asking a bankruptcy judge to approve a plan that divides whatever assets you have among your creditors (the people and businesses you owe money). You may also be asking the court to discharge or cancel your debts if you do not have enough money or property to pay the debt. In return for a very visible and long-lasting black mark on your credit record, bankruptcy allows you to pay what you can to your creditors and walk away from your debts.

Under changes to the federal bankruptcy code in 2005, you may be required to obtain credit counseling before filing for bankruptcy. If you choose to proceed, you then work with an attorney to file for bankruptcy in federal court. The filing fees aren't very expensive. Attorney's fees vary widely. You and the court choose between two personal bankruptcy options: Chapter 7 and Chapter 13. The court reviews your finances and decides whether to allow you to file for bankruptcy, and which of the two bankruptcy options is right for you.

Chapter 7 and Chapter 13 bankruptcy

Chapter 7, known as *straight bankruptcy* or *liquidation*, is the more drastic step and historically has been the more common choice. (The 2005 bankruptcy code made it more difficult to gain a court's approval to file for Chapter 7 bankruptcy, and courts are steering more people to Chapter 13 bankruptcy.) Here's what happens in a Chapter 7 bankruptcy:

- If the court grants your bankruptcy petition, a court trustee decides which of your assets you can keep. These are called *exempt* assets. Different states have different rules about what you can keep in order to move on with your life. A federal code applies in all states, and you can choose whether to have your assets reviewed under the state or federal guidelines. Under the federal code, exempt assets include
 - a portion of the equity you have in your home (up to \$18,425 in 2004) if you commit to keeping up with mortgage payments
 - your car, truck, or motor vehicle (up to \$2,925 in value in 2004) or a small amount of equity in your car if you commit to keeping up with loan payments
 - jewelry (up to \$1,225 in 2004)

Half of those filing for bankruptcy have experienced a serious health problem. Two out of three have lost a job.

THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT
BY T.A. SULLIVAN, E. WARREN, AND J.L. WESTBROOK

This is not a complete list, just a sample to show some of the more commonly used exemptions. Basic household furnishings and work-related tools are also exempt in most states, for example. The dollar amounts are for an individual. If a married couple is filing together, the exemptions will be double. And the amounts are subject to change.

- Other high-value assets that do not qualify for exemption are turned over to the court trustee, who may then sell these assets at public auction and divide up the proceeds among your creditors.
- You are still responsible for certain debts and obligations: most student loans, overdue taxes, alimony, child support, and fraudulent loans. (A loan is considered fraudulent if you slightly exaggerated your income on the application or took any steps to hide a bad credit record.) These debts and obligations are still yours to pay even after the bankruptcy is final.

Chapter 13, a more limited form of bankruptcy also known as *reorganization*, allows you to keep all of your property while you repay your bills. It is similar in many ways to the process of working with a credit counseling service, only the court provides you with full legal protection from your creditors. You qualify for Chapter 13 bankruptcy by showing that you are employed and have enough income to pay reduced living expenses and repay your debts over time.

- If your petition is accepted, you submit a detailed budget to the court.
- The court reviews your budget, revises it, and turns it into a monthly debt payment plan.
- You are ordered to make debt payments directly to the court, and the court pays your creditors.
- If you fall behind in your payments to the court, you will be found in contempt of court and your case dismissed. You'll no longer be protected from your creditors. If you have no other options, you might then file for Chapter 7 bankruptcy (under which your non-exempt assets are turned over to the court and sold, with the proceeds going to your creditors).

Roughly one person or couple in every
72 American households files for
personal bankruptcy every year.

AMERICAN BANKRUPTCY INSTITUTE

When is bankruptcy the right choice and when is it not?

Bankruptcy is relatively easy. Roughly 1.5 million people file for personal bankruptcy every year. For some people, it's the sensible option. If a medical crisis kept you out of work or left you with extraordinarily high medical bills; if an accident or disease has left you with a disability that reduces your ability to earn an income; or if a divorce has left you with high debts, child care responsibilities, and a reduced income, your debts may be beyond your ability to repay.

But many people who file for bankruptcy are doing it for the second time. For people who've arrived at bankruptcy as a result of careless spending and a casual reliance on credit, bankruptcy can be seen as a quick fix that will solve a chronic debt problem. It's not. Bankruptcy doesn't get at the underlying root of a debt problem. Only you can do that. If debt spending is your problem, the only way to solve it is through a long-term commitment to debt reduction. It's your money behavior that needs to change.

The problems bankruptcy doesn't solve

Beyond the fact that it doesn't solve most people's debt spending problems, bankruptcy brings with it some other penalties.

- For the next ten years, your bankruptcy will be reported as part of your credit record when you apply for a loan, rent an apartment, or apply for a job.
- Your bankruptcy will be reported as part of your credit record forever when you apply for a job that pays more than \$20,000 a year or for a loan of more than \$50,000.
- When you look for a job, an employer may see your bankruptcy as a reflection on your character. It may be the deciding factor against you when you are compared to another candidate.
- When you look for an apartment, a landlord may see your bankruptcy as a warning that you'll fall behind in your rent, and can use that information when deciding to rent to someone else.
- You will find it very difficult to re-establish credit, at least for the next few years.

You might be able to get a credit card with a low spending limit—but with a requirement that you keep at least that much on deposit at the bank that issues the card. You might be able to lease a car—if you are able to pay 70 percent of the total value of the lease up front.

- The Internal Revenue Service gets a report of the bankruptcy settlement and considers as income any debt from which you are released. You will owe income tax on that amount.

Bankruptcy has its place. For people who have gotten into financial difficulties that really are beyond their ability to resolve, it offers a way to make a fresh start on sound footing. But without changes in financial behavior, it can extend money problems into a lifetime of juggling and worry.



What you should
know about
your credit record

If you've fallen behind in your payments, that information is probably being reported in your credit record.

What is a credit record? And why should you care?

Whenever you apply for a loan or a charge card, and many times when you apply for an apartment or a job, someone will check your credit record to see if you have a history of paying your bills on time. Your credit record shows all of the loans and credit accounts you've had for the past seven years and records every late payment. Bankruptcy is included as part of your credit record for ten years, as are other legal judgments against you. When you apply for a job that pays more than \$75,000 or for a loan or life insurance policy of more than \$150,000, there's no time restriction on your record—the employer, lender, or insurer can get a report on your credit history for your entire life. So a bad credit record can keep you from getting a loan, an apartment, or a job for a very long time.

A good credit record can make you look impressive to a potential employer or lender. A bad credit record can make you look irresponsible and untrustworthy.

Thanks to the Fair and Accurate Credit Transactions Act (FACTA), signed in 2003, every U.S. citizen is entitled to a free credit report once a year from each of the three main credit reporting bureaus: Equifax, Experian, and TransUnion. There are three ways to order your credit reports: online, by phone, and through the mail.

To order your credit report online, go to *www.annualcreditreport.com*. This centralized Web site sponsored by the three main credit bureaus allows you to order all three reports and view them instantly online.

To order your report over the phone, call 877-322-8228. Your credit report will be mailed to you within 15 days.

To order a report by mail, you will need to fill out an Annual Credit Report Request Form. You can find this form online at <https://www.annualcreditreport.com/cra/requestformfinal.pdf>. Then mail the form to:

Annual Credit Report Request Service
P.O. Box 105281
Atlanta, GA 30348-5281

When you get your reports, look them over carefully. If there's anything you don't understand, call the credit bureau for an explanation. The reports include a lot of information and you may need some help interpreting them the first time you see them. Federal law requires that the bureaus make this help available to you.

If you find a mistake in any of the reports, you have the right to dispute it and try to have it corrected. Ask the credit bureau for a dispute form or send a letter with the correction you are suggesting. Attach copies of any supporting documentation (not original documents). Clearly identify each item in the report that you think is mistaken and explain why you think it is wrong. The bureau will respond in writing in about four weeks. It is the credit bureau's responsibility to prove that the information is correct, not yours to prove that it is wrong.

If the bureau investigates and finds that a mistake has been made on your record, the bureau will correct it. You can then ask the bureau to send a corrected version to anyone who has received your report within the past six months—and to any employer who requested a copy of your report as part of a job application process in the past two years. You can also ask the bureau to identify the source of the mistaken information, and you should send a letter explaining the mistake to that source, too.

If you're having problems with debt and have fallen behind on payments to any of your creditors, it's probably not mistakes on your credit record that will be your problem. It will be the detailed evidence of your late and missed payments. The only remedy for this is to improve your payment record, starting now.

Avoid credit repair services

You've probably seen ads for credit repair services and may have received their fliers in the mail. As you look for legitimate credit counseling help, you may come across their listings in the phone book. Credit repair services push an almost magical solution: "We'll wipe away your bad credit history and let you start over with a clean slate. We'll give you a new identity and let you step away from your old one. We'll remove bankruptcies, judgments, and bad loans from your credit file forever!"

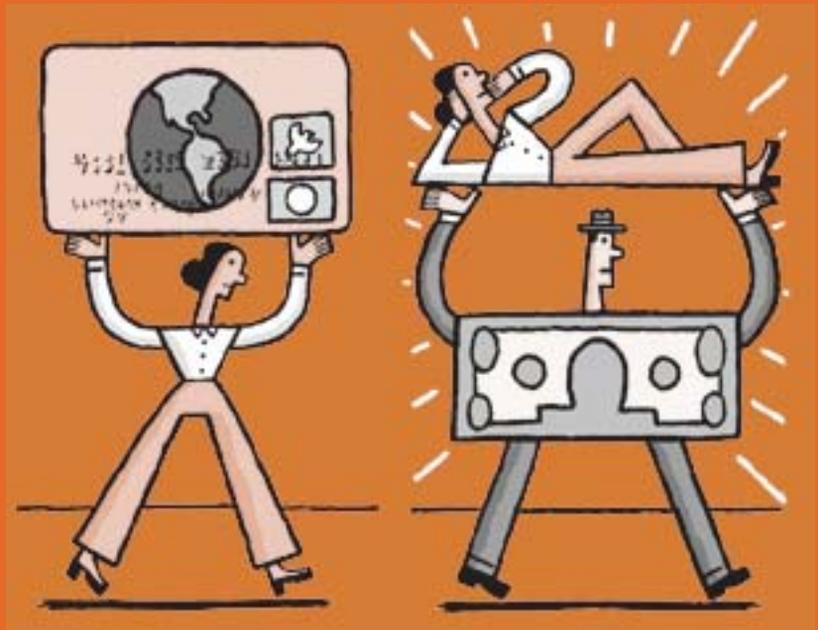
Stay away from them. They'll take money—hundreds or even thousands of dollars—that you desperately need to work your way out of debt. And they can't deliver. By the time you realize you've been taken, your money will be gone. And, in many cases, so will the credit repair service. Many of these services engage in illegal practices and come and go under different names until they are finally caught and shut down.

Here's what they usually do:

- Require you to pay up front, before any services are provided
- Hide important facts from you, such as your legal rights and what you can do yourself—for free—to correct mistakes in your credit record
- Suggest that you try to create a new identity for yourself by applying for an Employee Identification Number to use instead of your Social Security number on credit applications
- Get you to dispute all negative information in your credit report, even information you know is true

You can be charged and prosecuted along with the service for the part you play in any illegal actions they've suggested. It's a federal crime to make false statements on a loan or credit application, to misrepresent your Social Security number, or to obtain an Employer Identification Number from the Internal Revenue Service under false pretenses.

You are entitled to insert a statement of up to 100 words in your credit record explaining any late payment or credit problems. You might use this right to explain a stretch of money problems that were the result of a job loss, illness, divorce, or some other setback. You might also use it to explain that a particular bill wasn't paid because service wasn't completed or the merchandise was defective. You might also use the statement to explain that you recognized a debt problem at a certain date, and have committed yourself since then to improving your credit record. If the credit record shows an end to late-payment problems at that time, this statement and the evidence of your commitment to solving your debt problems will go a long way toward repairing your record.



Making your money
work for you

If you stick with your spending plan and keep applying the money you save to reducing your debt, there will come a time when you have no debt. The emotional burden that's been weighing you down will be lifted. When you have no debt or low levels of debt, you can really start making your money work for you instead of against you. Instead of working to reduce your debt, you'll be working to build your net worth.

Some of these steps are for the future, but some can be part of your money plan even if you're just starting to work on your debt.

Start a savings account

Building a savings account for emergencies is the first place to start. If you look back at the commitment you made on page 30, you'll see that only half of the money you found in your spending plan is going toward bigger payments on your debt. The other half goes to build an emergency savings reserve. Set up an arrangement with your bank to have this amount deducted from your paycheck and added to a savings account. It's important to move it out of your checking account and into a savings account so that you aren't tempted to dip into it for regular monthly expenses.

As this account grows over time, you can use it as a reserve for those big unexpected expenses that would otherwise push you back into debt—car and home repairs, dental bills, taxes, and other surprises. And it will be your protection from financial disaster if your income is ever interrupted. Make it a goal to build an emergency fund that's equal to three months of your current monthly expenses if you're in a two-earner household, or six months of expenses if you're the only wage-earner.

Once you've built a comfortable emergency fund, shift the monthly savings amount back to debt reduction. Until you've eliminated your high-interest debt, it doesn't make sense to put too much money in a lower-interest savings account.

“Money is better than poverty, if only for financial reasons.”

WOODY ALLEN

Start a retirement account

After your emergency savings account, retirement savings should probably be your next priority. You may be able to get started on this, too, while you're still working down your debt. Tax laws are designed to encourage retirement savings. If you're not investing in an Individual Retirement Account (IRA) on your own or a 401(k) or 403(b) retirement account through your employer, you're missing out on one of the best deals going. You put money into a retirement account before income taxes are taken out of it, so a bigger chunk of your earnings goes into your account to earn interest for your retirement. If you start investing when you're young, even modest contributions can turn into significant savings. If you put \$100 a month into a retirement account that earns interest or grows in value at a rate of 9 percent a year, you'll end up with roughly \$20,000 in ten years, \$65,000 in 20 years, and \$185,000 in 30 years. Because the money is taken out of your paycheck before you get it, and because there are penalties for early withdrawal, retirement accounts turn out to be the one savings method that really works for most people.

Save for your next big purchase instead of relying on debt spending

Before making a big purchase (a car or a major household appliance), figure out what you can afford in monthly payments. Try making those payments into your savings account for a few months before you buy. You'll find out if you can handle the monthly expense, and you'll have a big down payment toward the purchase. Better yet, delay your purchase for a few more months and pay in cash.

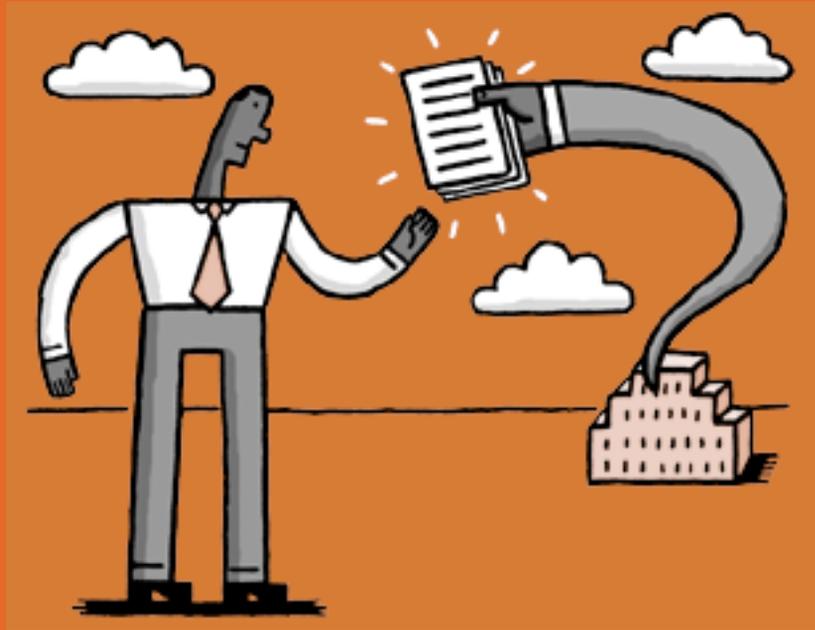
Buy insurance to protect your family's finances

Insurance should be an important part of your financial plan. Without it, you run the risk of facing huge expenses that could wipe out all of the gains you've so patiently made. And you could leave yourself or those who depend on you in financial ruin if something unforeseen were to happen. Here are some things to consider when looking at insurance:

- Health care is extremely expensive and is the cause of many bankruptcies for those without adequate insurance. Be sure you have health insurance that covers unforeseen physical and mental health needs for you and your dependents.
- Life insurance protects your family from the loss of your income if you were to die. Look for *term* life insurance (which is far less expensive than *whole* life insurance) and buy enough coverage to pay for your funeral and to cover your survivors' living expenses for three to five years.
- Buy disability insurance. Statistically, we are more likely to become disabled during our working careers than we are to die before we retire. And a disability can be very costly to you and your family. Not only is your income reduced, but you may incur higher medical and living costs, as well. Consider the percent of your income (60 or 70 percent) that the policy will cover. But also look at how it defines a disability. Some policies make it very difficult for a person to qualify as disabled.
- Buy automobile, homeowner's, and umbrella liability insurance appropriate to your family's situation (\$100,000 per injury, \$300,000 per accident, and \$50,000 in property damage is the minimum automobile coverage most people should consider). Don't assume that the minimum required by your state or the most basic policy offered will be enough for you.

Buy your own home

Buying your own home turns housing from an expense into an asset. Instead of being at the mercy of rent increases over time, your costs will stay flat or decrease as you pay down your mortgage. Mortgage interest and property taxes are tax deductible, which makes the cost of home ownership more affordable. And if property values increase, you'll own a growing asset.



For more
information

Financial counseling

If your employer offers financial counseling as part of your employee benefits package, this is a good place to start looking for help and information. Check with your Human Resources department, a union representative, or the program that sent you this booklet to see if financial counseling is available to you.

Nonprofit credit counseling services are available in most communities. Look for a service or agency that is certified by the National Foundation for Credit Counseling (NFCC). The NFCC offers a directory of member agencies, which you can access by phone at 800-388-2227 or online at www.nfcc.org.

Support groups

Debtors Anonymous
General Service Office
P.O. Box 920888
Needham, MA 02492-0009
781-453-2743
www.debtorsanonymous.org

For a meeting list or help in forming a chapter in your area, send a stamped, self-addressed envelope. See page 37 for a description of this organization.

Publications and written information

Federal Trade Commission
Bureau of Consumer Protection
Office of Consumer and Business Education
877-FTC-HELP
www.ftc.gov

Offers helpful articles on managing money and dealing with debt problems and information on avoiding frauds and illegal credit help services. Click on “For Consumers” on the site’s home page.



Daily cash spending log

Use these tear-off sheets to track cash spending for two weeks.
(See page 17.)

RECORD ALL EXPENSES

MONDAY EXPENSES

TUESDAY EXPENSES

WEDNESDAY EXPENSES

Groceries/meals

Tolls/parking

Gas

Clothing

Newspapers/magazines

Dry cleaning

Gifts

Kids' allowance

Other

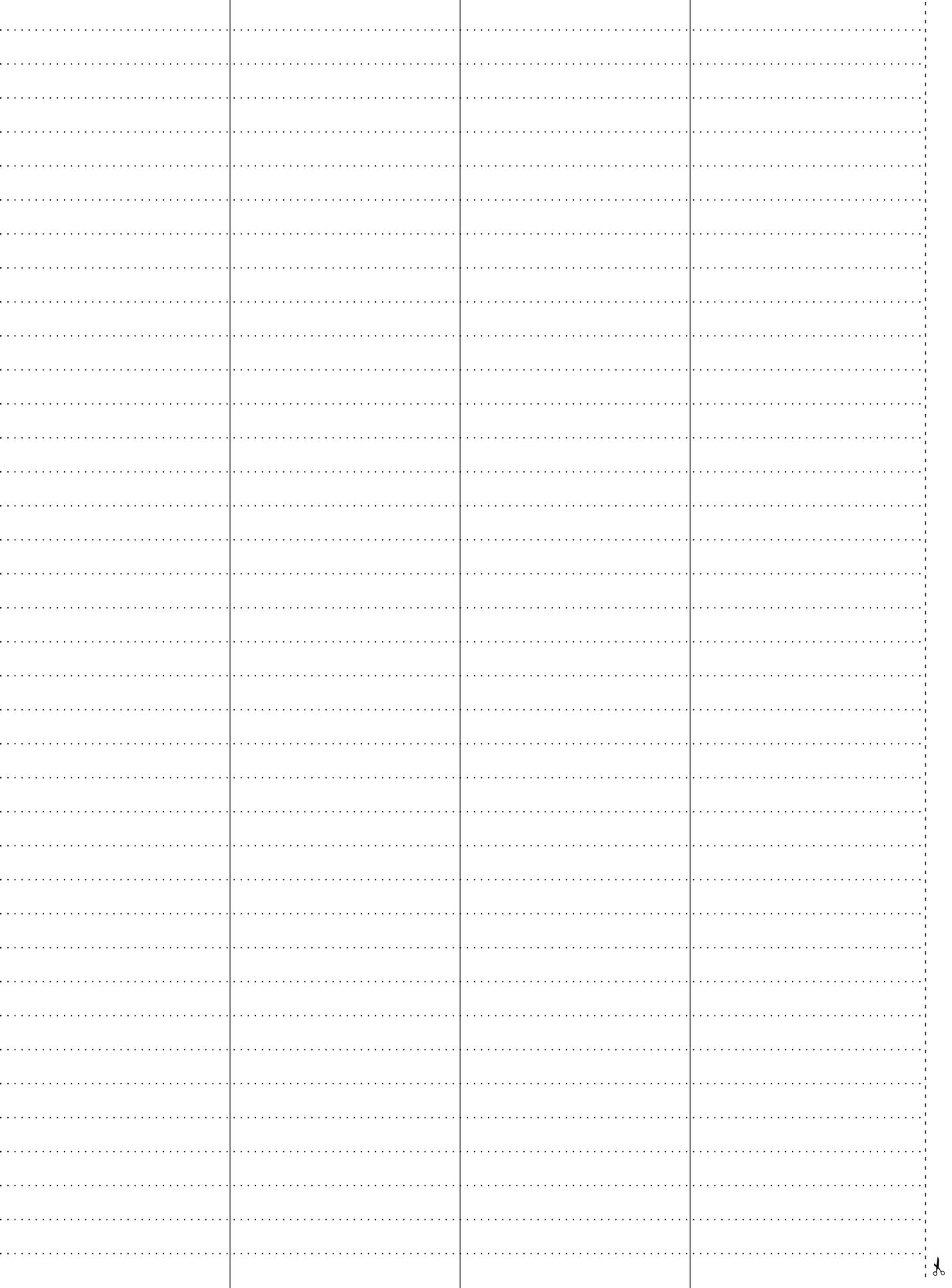
THURSDAY EXPENSES

FRIDAY EXPENSES

SATURDAY EXPENSES

SUNDAY EXPENSES





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MONDAY EXPENSES

TUESDAY EXPENSES

WEDNESDAY EXPENSES

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Tolls/parking

Gas

Clothing

Newspapers/magazines

Dry cleaning

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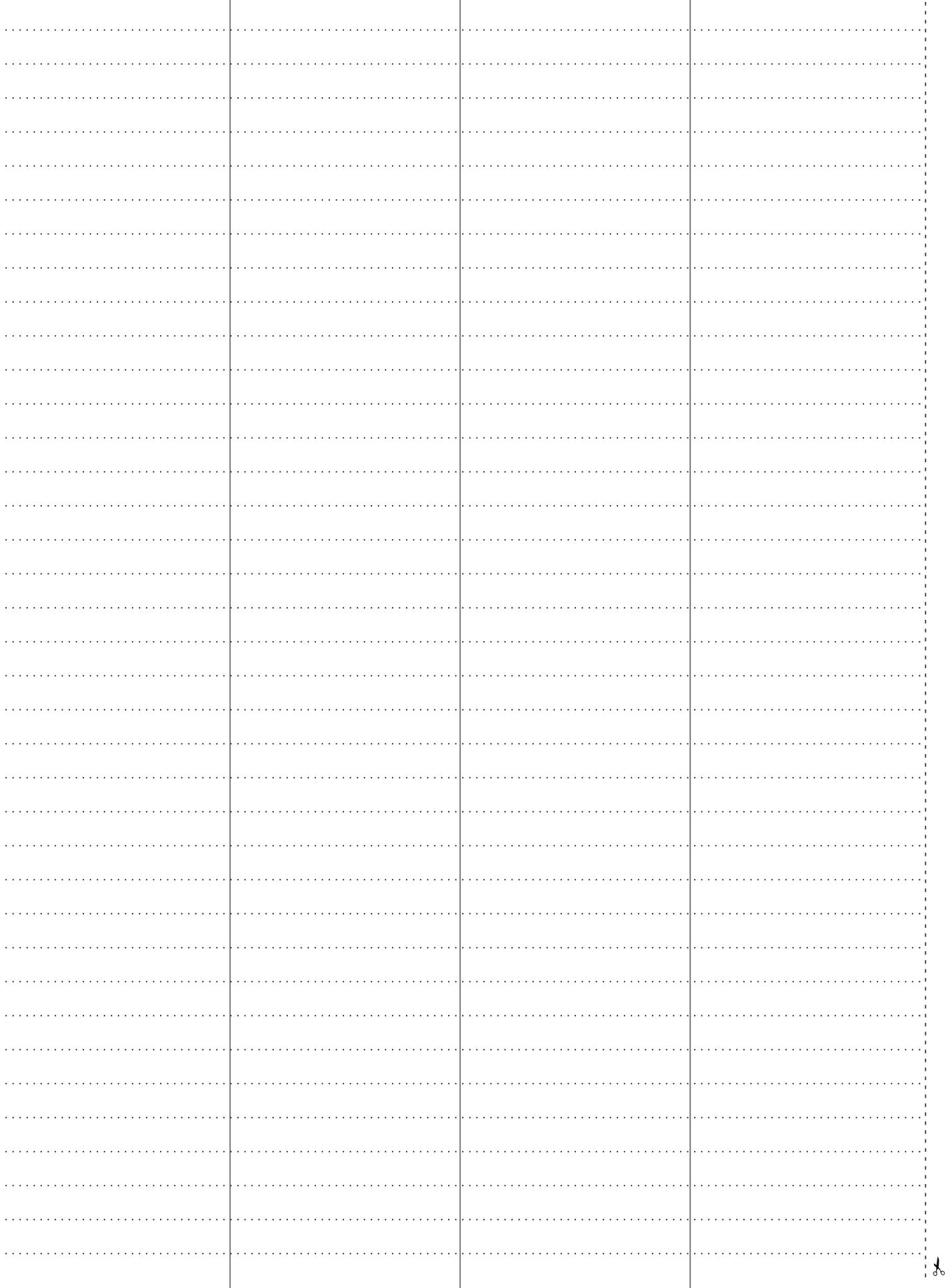
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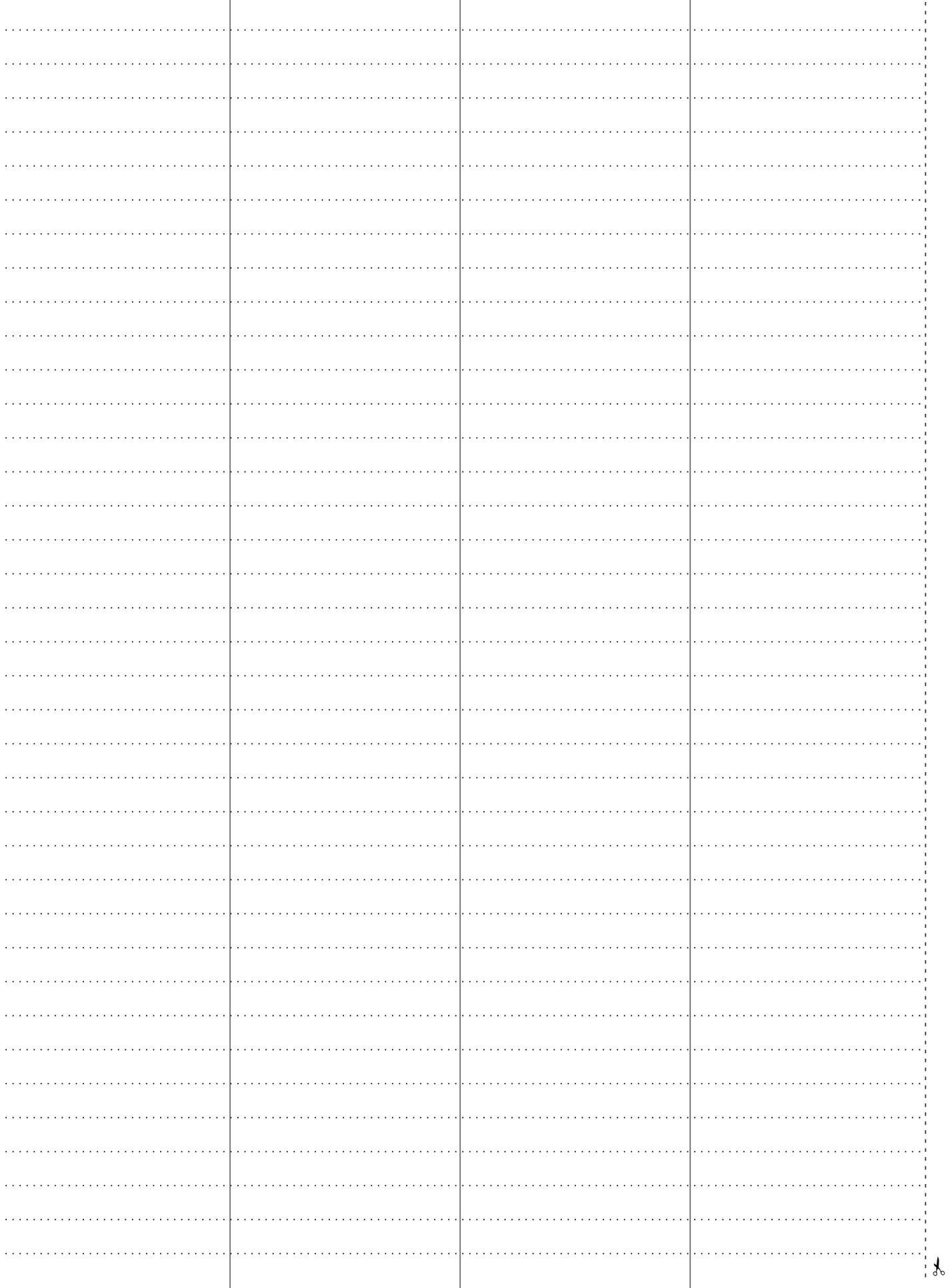
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SUNDAY EXPENSES





We'd like to hear any ideas you have for improving this booklet.
Please send us your suggestions at publications@ceridian.com.
Be sure to include the title of the booklet in your message.

Thank you.

Four steps to reduce your debt

1

Admit that you have a problem and commit yourself to fixing it.

2

Stop debt spending.

3

Make a spending plan.

4

Pay down your debts month by month.
Pay them off one by one.