

Managing Debt

Watch out for debt! When you're getting ready for retirement, too much debt creates roadblocks that could cost you both time and comfort in your retirement years.

When you owe money—whether it's on a credit card or a mortgage—you are in debt. There are several types of debt. The most common ones are probably a mortgage, a home equity loan or line of credit, a car loan or personal loan, and a credit card balance. When these bills, along with your usual living expenses, add up to more than you can pay every month, it's a warning sign that you need to stop the slide into more debt.

If you're not sure how well you're managing your debt, ask yourself these questions:

- ❖ Am I spending more than my income on a regular basis?
- ❖ Do I spend more than 20 percent of my monthly income on debt other than my mortgage?
- ❖ Do I carry a balance on one or more credit cards?
- ❖ Do I tend to pay only the minimum required on credit card bills?
- ❖ Have I maxed out any credit cards?
- ❖ Do I borrow money from one credit card to pay on another one?

Out-of-control debt can have long-term effects on your future: You could lose your home, get a bad credit rating that prevents you from getting loans—or even a new job—and you could end up without enough retirement savings. So, answering “yes” to one or more of the questions above means you need to get your debt under control as soon as possible. To get control, you need a clear picture of your current debt and the options for lightening the load.

Add Up Your Debt

The first step to managing your debt is making a list of what you owe, and how much you're paying out each month. Use a worksheet to track your monthly spending (see sample inside).

- ❖ Mortgage—The interest rate on an adjustable rate mortgage (ARM), for example, can go up on a schedule that you agreed to when you signed the loan documents.
- ❖ Auto loan—The “finance charge” is usually a fixed interest rate.
- ❖ Home equity loan or line of credit—Your home equity loan will have a fixed interest rate, but if you have a Home Equity Line of Credit (HELOC), the rate may have risen since the last time you looked.
- ❖ Personal loans—Be sure to check the rate on loans you may have from a bank, credit union or other financial institution. Keep up the payments so you don't end up with late fees.
- ❖ Credit cards—Credit card rates can also vary tremendously. They may range from the special zero percent rate you received when you applied for a new card, to 20 percent or more.

Look at your monthly statements to see what interest rates (finance charges) you're paying on each of these. If you haven't paid attention for a while, you may find you're paying higher rates than you thought.

Spending Worksheet

First, **write down your expenses**. Column A: *fixed expenses*—monthly cost, if the payment varies, write in an average. Column B: *flexible expenses*—costs that can vary month to month, and that you have some control over.

Expense Category	Expense Item	Column A Fixed Expenses	Column B Flexible Expenses
<i>Samples</i>			
<i>Entertainment</i>	<i>Restaurants</i>		\$200
<i>Home</i>	<i>Rent</i>	\$600	
<i>Home</i>	<i>Water/Sewer</i>	\$ 50	
Housing	Rent/Mortgage/Taxes		
	Maintenance/Condo fee		
	Lawn/Garden		
	House Cleaning		
Utilities	Electric		
	Gas/Oil		
	Water/Sewer		
	Garbage		
	Phone		
	Internet Account		
Food	Groceries (average)		
	Restaurants		
	Snacks (coffee, etc.)		
	Entertaining (food/beverages, etc.)		
Transportation	Car payment/Lease		
	Gas		
	Car Insurance		
	Subway/Bus/Parking		
Medical	Health Insurance		
	Regular Prescriptions		
	Out-of-Pocket		
	Fitness Programs		
Appearance	Clothing Purchases		
	Dry Cleaning		
	Hair Care		
	Miscellaneous		
Other			
Childcare			

Expense Category	Expense Item	Column A Fixed Expenses	Column B Flexible Expenses
<i>Samples</i>			
Entertainment	Movies/Videos		
	Newspapers/Books		
	Cable TV		
	Sports (Golf, etc.)		
	Theatre, Concerts		
	Travel, etc.		
Savings	Retirement Contributions		
	Other Savings		
	Reserve Fund Contributions		
Creditors	Credit Cards		
	Other		
Other	Business expenses/ Alimony		
Total			

Now, write down what comes in every month. Make sure to enter after-tax income:

Income Source	Your Income	Your Spouse or Partner's Income	Total
Salary/Wages from employment			
Income from Self-Employment			
Rental Property Income			
Alimony			
Monthly Investment Income			
Social Security Retirement Benefit			
Social Security Widow/Survivor's Benefit			
Pension Benefit			
IRA Income (distribution)			
Veteran's Pension			
Annuity Income			
Inheritance/Trust			
Gifts			
Other			
Total			

Now, do the math. Add Column A and B from the first table, and subtract the total from the second table:
 (Income – Expenses = Potential Savings to help reduce debt)

Prevent More Debt

If you realize you're in debt, search for ways to cut your expenses right away. You can prevent your debt from growing by breaking habits such as eating out a lot, driving the car when you could take the bus, leaving the lights and the heat on when you're not in the house, and buying clothing or other things you really don't need.

For people who depend heavily on plastic to pay their daily expenses, the best way to cut spending is simply to get rid of the credit cards and pay with cash. If you can't afford to pay cash for necessary, large purchases, shop carefully to get the best deal. (For more suggestions on how to reduce your expenses, see the AARP financial publication, "Cost Cutting.")

If you are struggling with your mortgage, you may be eligible for special help under the "Making Home Affordable" plan. Visit www.makinghomeaffordable.gov for information on refinancing and mortgage modification.

Tips for Reducing Credit Card Debt

The average American has \$11,000 in credit card debt. Here are some steps to take to reduce this type of debt:

- ❖ Call the credit card company and request a lower interest rate.
- ❖ Pay more than the minimum every month.
- ❖ Put all of the debt on one card with the lowest interest rate you can find. Moving the debt from one card to another is called a "balance transfer." To make sure a balance transfer really lowers your payments, ask these questions: Is there a service fee for the transfer? Will they charge you the lowest rate on the balance transferred? How long will the current rate last? What is the rate for new purchases?



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- ❖ Before getting a new credit card for any reason, compare rates on your options, and ask how long the rate will be in effect.
- ❖ Never miss a payment. Even if you're just a few days late, you may be charged a late fee, your interest rate may go up, and your credit rating may be affected.
- ❖ When you cancel a card, do so in writing and keep a record of the cancellation.

Your To-Do List:

- Calculate your monthly expenses and income using the Home Budget Calculator at www.aarp.org/money. Look under "Tools."
- Find creative ways to cut your spending.
- Pay down high-interest credit card debt first.
- To learn how debt can impact your credit rating, visit www.consumerfed.org and click on "Consumer Information," then "Credit and Debt."
- Learn how to select the right credit card(s) for you, at the Federal Reserve Board website www.federalreserve.gov/creditcard.
- Start an emergency fund after you've paid down the high-interest credit cards.
- Use a debt reduction planner. LifeTuner, an AARP online initiative, has a tool that can help you figure out the fastest way to pay off multiple debts. Go to www.lifetuner.org. Then look under "Tools," "Credit Cards & Debt," and "How Soon Can I Pay Off My Credit Card?"
- If you need help with debt problems, learn how to choose a reputable credit counseling service at www.aarp.org/debtchallenge. Scroll to the article called "Debt Management vs. Debt Settlement: Which is Best?"
- Check to see if you are eligible for one of the "Making Home Affordable" options if you are struggling with your mortgage at www.makinghomeaffordable.gov.
- Order other AARP financial publications at www.aarp.org/orderfinancialpubs.

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