GOLD VISION FINANCIAL SERVICES

DEBT AND MORTGAGE REDUCTION INFO SHEET

Warning - None of the following is going to work without discipline and a budget. Failure to set a budget, review your spending and stick to your plan will just see you **FAIL** in achieving the reduction/elimination of your debts.

Setting a Budget

By working out your financial budget and reviewing it on a regular basis you will be able to manage your finances, identify areas where savings can be made and apply those savings towards lifestyle and debt commitments. If you continue to have difficulties in maintaining a budget then you should seek further advice from a financial counsellor.

To set a budget – simply write down every expense including daily, weekly, monthly and yearly. Review it, identify where savings can be made by changes in lifestyle or spending habits, and then divide by your pay period ie weekly fortnightly or monthly. This will then provide you with an amount you must set aside for both short term and long term expenses.

You can further assist management of the above expenses by putting aside long term expenses such as car repairs, medical, car registration etc into a separate bank account and only drawing on it for such expenses.

Whatever is left over after expenses should then be used for either debt reduction and/or investments.

It is **important** to review your expenses on a regular basis to see if you can get a better deal or discount as things change over time. It is also important that you review your expenses and debt management on a regular basis and this may be weekly at first until you train yourself to be efficient in the financial management of your affairs.

There are many examples of cutting down on expenses such as:

Bulk purchase groceries when on special
Considerable savings on beer purchases by home brewing.
Stop smoking
Stop or reduce eating out
Pay bills upfront or annually
Take your lunch to work
Take water and sandwiches when going out with the family.
Review telephone and internet contracts or packages on a regular basis
Make a shopping list
Buy second hand clothes, toys, used cars etc.

Remember, the most important thing to remember is to monitor and review your budget on a **regular basis!**

DEBT REDUCTION

The following ways may be used to reduce debt:

Make Additional Contributions

By making additional payments on the smallest debt first, whilst maintaining the minimum required payment on the remaining debts, you will reduce and pay off the smallest debt in a shorter time frame. Once this debt is finalised, then roll over the additional payments plus the existing debt payment onto the next smallest Debt. Once this Debt is finalised, then continue to rollover those payments onto the next smallest debt and continue this process as each debt is finalised.

The result of this Strategy is to reduce Principle quickly on one debt at a time and therefore the amount of interest charged – thus reducing the time frame in paying off debt.

Payment of High Interest Debt first

By paying off high interest debts first you will reduce the amount of interest paid and therefore reduce the time frame in paying off debt.

For example, if you have two debts of $ 1,000 with interest rates of 5% and 30% then by paying off the debt with an interest rate of 30% first, you will reduce the amount of interest paid and therefore reduce debt levels at a quicker rate.

This Strategy combined with making additional contributions is an effective Strategy in reducing the time frame in paying off debt.

Convert High Interest Debt to low Interest Debt.

By converting high interest rates on debts to lower rates, you may save substantial amounts in interest incurred on your debts. Some Credit Cards may have an interest rate of 30% per annum. By converting these credit cards to a low rate card then you may save 20% or more in interest being applied to your account. For example 30% interest on a balance of $ 1,000 will incur $ 300 per year in interest being applied to the account as opposed to only $ 100 per year on a credit card with at a rate of 10%.

This strategy will reduce the minimum monthly payment and therefore improve cash flows.

Special Discount Rate Offers

Some credit card or Lenders may offer short term special discount rates to entice you to transfer balances to their product. In some case they may offer 0% or very low interest rates for 6 – 12 months. By transferring your current debt you will save considerable interest on your debt during the discount period.

You need to assess what the rates will be when the discount period is expired and what ongoing charges are applicable. In some cases with Credit Cards you may be transferring from a low rate card to a high rate card or be incurring considerable higher charges, therefore, when the discount period expires you will be paying more than you are currently.

This strategy will reduce the minimum monthly payment and therefore improve cash flows. However, if you use the new facility during the discount period, you may find that your discount period may expire or that you are paying the standard higher interest rate on the new transactions. Therefore there may be no benefit in transfer balances over to another card if you are going to continue using the card.

Maintain Current Payments

Whenever interest rates or the minimum payment is reduced, if you are able to afford continuing to make payments at the current rate then you will in effect be making additional payments on the debt. This will have the same benefits as outlined above for additional payments.

Make Weekly/Fortnightly Payments

By making weekly/fortnightly payments instead of Monthly payments you will reduce debt levels in the following ways:

- you will be making additional payments over a year than if you pay monthly (you will need to be mindful that the weekly/fortnightly payments cover the minimum monthly payments) and

- you will reduce the principle balance each week/fortnight and therefore reduce the amount of interest applied to the account each month. For example, a mortgage over 30 years may be reduced by 3 – 4 years alone by making fortnightly payments.

This strategy can be used for any debt repayments.

Consolidate/Refinance Debts

To improve cash flows and/or reduce interest rate levels it may be appropriate to refinance or consolidate a number of debts into one debt. This may reduce minimum debt payments and therefore improve cash flows and/or it may also reduce the amount totally payable if a lower interest rate is achieved on some or all of the pre-existing debts. Refinancing may also result in the debt repayments being extended for considerable longer terms or periods and therefore may, over the longer term, continue to cause financial hardship.

If you have a large number of credit cards or loans then you may have difficulty in obtain refinancing as lenders are reluctant to refinance large amounts of debts.

Warning: some lenders who offer debt consolidation do so in conjunction with a Part 9 Debt Agreement which is a form of bankruptcy. Ensure when making enquiries that this is not the case as it will have severe implications in you obtaining future credit for up to 7 years.

Warning: Whilst this can be an effective strategy in improving cash flows care needs to be taken that you are not simply extending the time frame that you are in financial difficulty, incurring additional large fees or increase dramatically the amount to be repaid in total over time. Special care needs to be taken to ensure you are NOT dramatically increasing the overall debt to be repaid over the new repayment period.

Example: You have a car Loan of $ 20K at interest rates of 10% with payment of $ 500 p/m and a home loan at interest rates of 5% with payment of $ 500 pm being a total of $ 1,000 pm. You then consolidate your car loan into your home loan thus increasing you home loan payments to $ 650. However, the $ 20K car debt now is being repaid over 30 years which may see you effectively repay $ 40 k plus back over time as a result. However; if you maintain your current payments at $ 1,000 and apply them to the home loan you will achieve further savings as the effective interest rate on the car loan proportion is now only 5%.

Management of Debt Payments in Arrears

There can be severe consequences in not maintaining your debt payments including Notifying Credit Reporting Agencies, Legal Action, Seizure of Goods and Bankruptcy Proceedings. The cost of this is normally passed on to you. Those actions may adversely affect your ability to obtain credit in the future even though the personal circumstances at the time have now been resolved. Financial hardship and subsequent actions by credit providers to recover monies owed often cause emotional distress on you and your family.

In order to prevent recovery action, please ensure that you make adequate payment arrangements with the provider to bring your account back to an acceptable level. Most providers will accept short term payment arrangements without recovery action being needed. However, where short term arrangements are not acceptable to the lender then you may need to consider the following:

- Most providers have **Hardship Provisions** where they can make longer term arrangements to allow you time to rectify your circumstances and this may include lower payments, reduction of interest or no interest being applied to your account or a combination. It is important that if you can not enter into short term payment arrangements that you are referred to the Providers Hardship Department who have more authority to deal with the issues.

- **Access to Superannuation.** In certain circumstances including Compassionate grounds and Financial Hardship, you can apply to have part of your Superannuation released to meet ongoing financial commitments or Debt arrears. You will need to speak with your Credit provider and/or your Superannuation Fund as to whether you will qualify for this release. Note that if the release of funds is not in conjunction with an ability to meet future debt payments then the credit provider may refuse to accept a release of super funds.

Sale of Assets Combined with the Restructure of Associated Debt

Depending on resale values, in some cases where there is equity in an item under finance such as a car or the value of the item is of higher value and the amount owing is NOT lower, then consideration may be given to the sale of the item. You can then purchase an item of a lower valued item whether from proceeds of the sale or through more affordable finance.

Care should be taken in considering this Strategy especially if resale values are considerably lower than the existing total debt. You should always get a payout figure prior to making this decision and enquire about break out costs, capital gains, sale agent fees, stamp duties and capital tax.

In some cases there may be no option but to sell an asset such as a car or a house and reverting back to renting or operating one car within the household. **Further Financial Advice should always be sort in these circumstances.**

MORTGAGE REDUCTION

Mortgage reduction can be achieved in the following ways:

1. Make a monthly payment at the draw down (initial settlement) of the loan. This ensures that your account is already in credit from day one and that a month's worth of interest has not been applied to the account before you make your first payment. This is not applicable to those who have already commenced payments on their Home Loan.

2. Make Weekly or fortnightly payments. This will normally save you at least 3 years payment on a 30 year loan in the following ways:

a. This results in the principle during the month and thus reduces the amount of interest being accrued each month, and

b. You will be making an additional 4 weeks of payments as there are 26 fortnight/52 weeks rather than 12 monthly payments (24 fortnights/48 weeks).

3. Use of an offset Account. An Offset account is a separate bank account that is linked to your home loan where the balance of the account is offset against the balance of your home loan. Whilst not reducing the physical balance of your home loan it does reduce the amount of interest applied on your home loan by the balance held in you offset account. Using an offset account to receive income such as pay and then using the account to make expense / lifestyle purchases such as food etc you can save a further 1 – 2 years in home loan repayments.

Ie if your home loan is $ 300,000 and your offset account has a balance of $ 1,000 then the interest applied on your account is worked on a home loan balance of $ 299,000 not $ 300,000. At 6 % interest rates this will save you around $ 5 in interest per month. You monthly payment will therefore reduce the principle by $ 5 with further ongoing interest savings over 30 years.

4. Using an offset account combined with a Credit Card. **Warning** you should not use this method if you **cannot** control credit card spending. Most credit cards provide a 30 – 40 day interest free period on purchases. By using you credit card for monthly purchases such as food and fuel and then paying off the credit card at the end of the month from your offset account, you maximise the amount of time your funds (incomes received such as pay) are held in the offset account.

This method takes a lot of discipline and careful monitoring of the use of the credit card; however, it will maximise the balance of your offset account and thus the benefit of using an offset account.

5. Applying extra additional payments. If you pay off a home loan with normal monthly payments you will pay up to or over 200% plus more back to the bank than what you borrowed. By applying extra payments on your home loan on a regular basis ie $ 50 per month and any additional bonus – such as employment bonus, proceeds from a win or inheritance you receive, you will reduce the loan term considerably.

Summary:

Mortgage and Debt Elimination can be complex and there is no easy fix. You need discipline to make it work and without adhering to your plan then you will fail. Beware of some of the traps outline above. If you need help do not hesitate to contact me via email john@goldvision.com.au or Australia 08 93758500

Cheers

John Horvath

Disclaimer:

The above is General Advice and does not take into account your personal circumstances. You should always seek the advice of a professional to discuss your personal circumstances.

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