How To Eliminate Debt

STEP 1 – TOTAL YOUR EXPENDITURES

Track and total 1) debt owed and 2) monthly payment for all of the following expense categories:

Mortgage Payments

Personal Debt Payments – expenses that *cannot* be canceled
Student Loans
Car Loans
Credit Cards
Lines of Credit

Non-Debt Payments – expenses that *can* be canceled
Utilities
Phone
Gas
Clothing
Food
Activities
Charitable Giving

Make sure that *every single expense* is documented. Options Financial Residential Mortgage encourages the use of a debit card ensure the documentation of all cash expenses.

STEP 2 – DETERMINE YOUR NET MONTHLY INCOME

Your **Net Monthly Income** is your take-home pay *after* taxes and other deductions, such as health insurance contributions, social security, saving plans, and garnished wages.

Keep in mind that your Net Monthly Income differs from your Gross Monthly Income, which is your take-home pay *before* taxes and other deductions.

Subtract your total expenditures from your Net Monthly Income to identify your **Total Spendable Income**

Total Expenditures - Net Monthly Income = Total Spendable Income

If your total expenditures are less than your net monthly income, you will have **Excess Spendable Income**.

If your total expenditures are more than your net monthly income, you will have a **Shortage in Spendable Income**.

STEP 3 – ELIMINATE UNNECCESSARY EXPENDITURES

By creating an awareness of your spending habits, many non-debt expenses can be reduced or eliminated. Common areas for improvement include:

Eating Out

Grabbing a meal away from your home may fit into your budget some days, but when you eat out every day, money can quickly be spent. Plan to pack your lunch or make meals at home.

Coffee

Do you *need* coffee? Can you make coffee at home rather than purchasing it from a vendor? If you are on the go, is there a cheaper drink you can order?

Clothing

Is it a necessity to purchase an article of clothing each week? Can you reduce the number of items you purchase? Is there a less costly clothing store?

Impulse Buys

Do you frequently buy unnecessary items? If you were fine without the item today, and will be fine without it tomorrow, it is likely you do not need to make a purchase. When going to the store, *make a list* and stick to it.

Can you realistically eliminate any of these expenses? If so, great! If not, how can you work to reduce your spending?

Now that you have evaluated your unnecessary expenditures, how much money will you be able to free up through the reduction or elimination of your spending?

STEP 4 – CALCULATE YOUR EXCESS SPENDABLE INCOME

Determine the maximum amount of money you can apply toward debt elimination. To do this, combine any excess funds you found in Step 2 with any funds you were able to free up in Step 3.

Excess Spendable Income + Freed Up Funds = Debt Elimination Investment

Remember! The more you can apply toward debt elimination, the faster you get rid of your debt all together! Think of this as your *Debt Elimination Investment*.

STEP 5 – DETERMINE HOW YOU WILL PAY OFF YOUR DEBT

When it comes to paying off your debt, you have a couple of options!

"Snowballing"

When using the Snowballing principle, your debts get paid off faster and faster until each debt is completely eliminated! Here is how it works:

Debt A – your *lowest* balance debt.

Apply your Debt Elimination Investment to your normal monthly payment for Debt A until it is paid in full.

Debt B – your *second* lowest balance debt.

Apply your Debt Elimination Investment and the monthly payment amount of Debt A to your normal monthly payment for Debt B until it is paid in full.

Debt C – your *third* lowest balance debt.

Apply your Debt Elimination Investment and the monthly payment amounts of Debt A and B to your normal monthly payment for Debt C until it is paid in full.

Each time you pay off a debt, your Debt Elimination Investment grows larger!

"DPR"

If you base your debt elimination on the Debt-to-Payment Relationship (DPR) of your individual debts, you can eliminate your debt even faster! Here is how it works:

Calculate the DPR of each debt.

Divide the current minimum payment of each individual debt by its current balance.

This will give you a percentage. For example, a car loan of $20,000 with a minimum payment of $400 a month would equal 2% DPR

Determine where to start.

To determine which debt to pay off first, list your debts in order of highest DPR to lowest DPR. The debt with the highest DPR should be paid off first.

Apply the Snowballing principle.

Move down your DPR list using the Snowballing principle explained above until all debt is eliminated!

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Your Debt Elimination Investment will continue to increase in this scenario as well! In addition to reducing the balance of each individual debt, the DPR method will also tackle interest reduction!

*Do not include your mortgage in debts to be paid off. Focus on everything else first, and we'll address the mortgage later!

STEP 6 – MAINTAINING FINANCIAL SUCCESS

Now you have the tools to pay off your debt! What else do you need to be successful?

Maintain the Debt Elimination Investment you establish.

As you eliminate individual debts, creating financial 'breathing room', you may be tempted to reduce your monthly debt payments. **Don't give in!** Reducing your monthly debt payments will dramatically extend the amount of time it will take to reach total debt elimination.

Do not add to/reopen debts.

You are in the process of eliminating the control debt has on your finances. If you use your credit cards, or charge on a card that has been eliminated, you are negating any gains you've made! This process requires great discipline. Remove any temptations to finance. Cut up credit cards. Close lines or credit so that you can no longer charge to them. Don't go 'window shopping' for unnecessary items you have eliminated from your budget!

Stick to your budget.

Remember, you've established this budget so that you can stay on track to eliminate your debt! Don't stray from your goal. If you have not yet created a budget, please refer to the Options Financial Residential Mortgage How To Budget guide available on our website.

STEP 7 – PAY OFF YOUR MORTGAGE

Once you have eliminated all other debts, you can apply the Snowballing principle to your mortgage loan!

With all of your freed up financial savings, you have the ability to make additional monthly payments toward the principal balance of your mortgage.

This will allow you to pay off your mortgage loan sooner – leaving you completely debt-free!