



Debt Repayment

**Cornerstone Foundation's Journey to Financial Wellness
(developed by the Financial Wellness Task Force)**

JOURNEY TO FINANCIAL WELLNESS



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HOW YOU BORROW



WHAT YOU WILL LEARN:

1. CREDIT VS DEBT
2. DEBT REPAYMENT METHODS
3. DEBT WORKSHEET

CREDIT VS. DEBT



When talking about money, the two words credit and debt tend to come up often. It is important to understand what each is, and how to manage both to improve your current and future financial standing.

CREDIT

Credit is one's ability to borrow money along with terms that one agrees to adhere to in **repayment**. Sometimes credit is used for things that you cannot pay for in full immediately, but instead agree to pay back over time, plus interest.

There are three types of credit: revolving, installment, and open debt.

Revolving debt, like a line of credit or a credit card, has a credit limit extended to you that you cannot exceed when making purchases. You can then choose to repay the amount in full monthly, or at least make a minimum payment. Any remaining balance unpaid beyond the minimum carries over to the following month, plus interest.

Installment debt is a loan for a set amount of money that you repay over a specific time period through fixed, regular payments that include interest and fees. Car loans and mortgages are common examples of installment debt.

Open debt typically applies when you have a contract or agreement with a company providing you a service that you pay for each month, like a utility bill. Your payment may fluctuate from month to month based on your behavior or how you use the service that month.

DEBT

While credit is money readily available for you to borrow, debt is money that you've already borrowed but haven't yet paid back in full. Credit is therefore a route to acquire a debt. The more credit that you choose to use, the more debt you acquire. When you can repay your debts in full, you do not accumulate **interest**, which is a percentage cost per dollar that you agree to repay as a fee for borrowing money.

TYPES OF DEBT

There are three different types of credit: revolving, open, and installment. Each form of credit is defined based on how debt is borrowed and repaid. Each also has a different impact on a credit report and varying importance in the monthly budget.



Revolving

A type of credit where you can borrow, pay off, and borrow again up to a predefined amount of money.

- Credit Cards
- Home Equity Lines of Credit



Open

Payments are due in full each month, and the amount you have to pay may vary based on your usage.

- Utility Bill
- Cell Phone Bill



Installment

A type of credit where you borrow an amount of money all at once and pay it back in predetermined chunks or installments.

- Car Loans
- Mortgages
- Student Loans

THINGS TO CONSIDER

Debt is a financial tool that can provide the opportunity to purchase items we want or need. It is important to be cautious when you use debt, as it can easily become overwhelming if overused or not used correctly. Here are some ideas to consider:

KNOW BEFORE YOU SIGN

Get familiar with your debt before you take it on. Here is a checklist of questions to answer before you sign a loan agreement:

- What is the **interest rate**? Are there annual fees?
- What will the payment be?
- How often are you going to make payments?
- How long will it take you to pay the loan off?
- Who do you contact if you have trouble making the payments?

IS THE DEBT MANAGEABLE AND AFFORDABLE?

Taking on too much debt can feel overwhelming, like facing an unscalable mountain. Before applying for new debt, it's crucial to review your budget to ensure you can accommodate the additional expense. By doing so, you can avoid financial strain and make informed decisions about your borrowing. Remember, managing debt effectively is key to maintaining financial stability and achieving your long-term financial goals.

Pro Tip: Practice Paying for the Debt

Before applying for debt, spend a month or two "practicing" by incorporating the potential debt payment into your budget. This will help ensure that the new expense fits smoothly into your monthly spending plan.





DEBT REPAYMENT

There are three great ways to repay debt, the Debt Snowball, Debt Avalanche, and Debt Consolidation.

DEBT SNOWBALL

The debt snowball method is a debt-reduction strategy that prioritizes paying off debt in order of those that hold the smallest balance to those debts that hold the largest balance. Think of paying debts off as a snowball rolling down a hill and gaining momentum and snow as it goes. The same is true with the snowball method, when the smallest debt is paid in full, that payment amount can now be rolled into your next smallest debt amount and so on. As you repay debts in full over time, you have more money to contribute to larger debts and the ability to contribute more to larger balances due.

DEBT AVALANCHE

The debt avalanche method is another strategy for paying down what might feel like a mountain of debt. This method involves paying off your highest-interest debts first, and then those with the next highest rate and so on. Make your highest interest debt your primary target while still making at least the minimum payments to all other debts. By using this method, you can potentially clear your debts more efficiently and minimize the total interest paid over time.

DEBT CONSOLIDATION

Depending on your debt situation, there could be opportunities to consolidate multiple debts to one payment. If you're a homeowner with equity in your house, a HELOC (Home Equity Line of Credit) or a cash-out refinance can both be great options to pay down high-interest debt. Regardless, the key to consolidating debt is making a plan to stay out of debt, so be sure your budget is locked in first!

REPAYMENT EXAMPLES



These examples illustrate how the debt snowball focuses on balances while the debt avalanche focuses on interest rates.

DEBT SNOWBALL

Creditor	Balance	Monthly Payment	Interest Rate	Due Date
Wells Fargo	\$765	\$30	27%	23rd
Cap One	\$1,123	\$35	26%	17th
Car Loan	\$3,725	\$235	7%	18th
Signature Loan	\$4,957	\$186	13%	5th
Discover	\$9,735	\$270	29%	15th
Totals	\$20,305.00	\$756		

DEBT AVALANCHE

Creditor	Balance	Monthly Payment	Interest Rate	Due Date
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DEBT WORKSHEET

Use the form below to create a list of your debts, including information about your balance, monthly payment, interest rate and due date. You can use this list to create a debt snowball or debt avalanche.

Creditor	Balance	Monthly Payment	Interest Rate	Due Date
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
	\$	\$	%	
Totals	\$	\$		

Pro Tip: One way you can elevate your repayment strategy is to use an online calculator to help you build a “debt snowball”, “debt avalanche” or a mix of the two. You can find a free debt repayment calculator by visiting www.powerpay.org. Enter your debt balances, payments and interest rates and let Power Pay create a guide to follow.



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