

FINANCIAL FIRST AID

Many circumstances in life can derail even the best money management plans and leave us with less money than is needed to meet monthly obligations. What can you do if you are in this situation? As tempting as it may be, the one thing you should not do is ignore bills and past due notices. The consequences of doing so can include:

- Higher interest rates on credit cards. Some creditors assess penalty interest rates well over 30%.
- Late fee charges.
- Credit report damage. Late payments can be reflected on your credit report for seven years.
- Repossession of loan collateral (such as a house or car).
- Loss of unpaid services (such as electricity or cable).
- Increasingly hostile and frequent calls from bill collectors.
- Garnishment of wages. (Most creditors have to take you to court before they can do this.)

The best way to handle a financial crisis is to review and adjust your budget, prioritize your financial obligations, and communicate with your creditors. You may not be able to pay all of your bills in full every month, at least not right away, but by taking a proactive approach to your finances, you can minimize the consequences until you get back on your feet.

STEP 1: Take Inventory of Income and Resources

If your expenses exceed your income, you will not be able to gain control of your financial situation until you make changes. Start by recording all of your sources of income, including realistic expectations of income that you will be receiving soon.

Think about ways that you may be able to increase your income. Some suggestions:

- If you own your home and have a spare bedroom, rent it out. A good place to advertise is nearby college campuses.
- Get a part-time job or work overtime if it is available. Ask family members who are able to work but currently are not to look for employment.

- If you regularly get a large tax refund, consider increasing the number of exemptions you claim on your federal W-4 form. This will increase your take-home pay. (However, be careful to not take so many exemptions that you have a large tax liability at the end of the year. It is a good idea to consult with a tax advisor or use the withholdings calculator on the IRS's website, www.irs.gov, before making adjustments.)

Make sure to apply for all benefits for which you may be eligible, such as unemployment insurance, food stamps, Social Security, or TANF (Temporary Assistance for Needy Families).

Monthly Income		
Source	Gross	Net
Job		
Spouse's job		
Part-time job		
Rental income		
Child support/ alimony		
Commissions/ bonuses		
Tax refunds		
Investment income		
Government benefits		
Support from family/friends		
Other		
Total		

Next, record the value of all assets.

Assets	
Source	Value
Checking/savings accounts	
Money market accounts/CDs	
Stocks/bonds/mutual funds	
Retirement plans	
Equity in house (market value - loan amount(s))	
Equity in cars	
Cash value of life insurance policies	
Furniture/collectibles	
Other	
Total	

You may be thinking, Should I liquidize some assets to pay for immediate expenses? That is certainly one option, but be aware that it may come at a cost. For example, withdrawing money from a retirement plan can result in taxes and penalties of up to 45% of the amount withdrawn. You are also leaving yourself

less money for the future. Still, the consequences of liquidating assets may be reasonable when compared with the possibility of losing your home or car. The important thing is that you not make these decisions lightly. Consider consulting with a financial professional who can help you look objectively at your options.

Liquidation is not necessarily the only way to utilize assets. Some retirement plans and cash value life insurance policies let you borrow against their value. You do not have to pay penalties or taxes when you borrow against a retirement plan as long as you do not default on the loan. If you own a home that has equity in it, you may be able to get money to pay the bills from a home equity line or loan or cash-out refinance. However, keep in mind that if you cannot afford the payments, you could lose your home.

STEP 2: Review Your Expenses

In the “Current” column of the Monthly Expenses worksheet, on the following page, list what you are currently spending your money on. Do not include expenses that are directly deducted from your paycheck.

Monthly Expenses					
Expense	Current	Proposed	Expense	Current	Proposed
Rent/mortgage			Tuition/lessons		
Second mortgage			Life insurance		
HOA dues			Union dues		
Property taxes			Storage fees		
Homeowners insurance			Beauty/barber		
Renters insurance			Movies/videos		
Gas/electric (house)			Sports/hobbies		
Water/sewer/garbage			Gym membership		
Telephone (land-line)			Vacation/travel		
Internet access			Books/music		
Cable/satellite			Clothing purchases		
Cell phone/pager			Laundry/dry cleaning		
Groceries			Pool/hot tub service		
Household items			Gardening		
Dining out/snacks			Alarm system		
Health insurance			Gifts/cards		
Co-pays (medical)			Pet care		
Car payment #1			Banking fees		
Car payment #2			Postage		
Gasoline			Cigarettes/alcohol		
Repairs (house)			Donations		
Repairs (cars)			Savings		
Auto insurance			Other		
Auto registration			Other		
Tolls/parking			Other		
Public transportation			Other		
Daycare/babysitting			Other		
Alimony/child support			Total		

Getting a part-time job or renting out a room is not a practical option for many people. However, almost everyone can reduce their spending in some way. Look over your worksheet carefully and consider what you can cut. Discretionary expenses, such as clothing, dining out, and vacations, are often the easiest to trim, but you may be able to cut spending in other places too. For example, if you have a cell phone, can you cancel your land-line, or at least extra features like call waiting and caller ID? Can you carpool, walk, or take public transportation more often to save money on gasoline? Can you reduce energy consumption (by turning off lights when you are not in the room, wearing a sweater instead of turning on the heater, etc.) to lower your utility bills? Do you have any club memberships, newspaper or magazine subscriptions, or cable services that you can cancel? Write what you think you can spend in the future in the “Proposed” column.

STEP 3: Take inventory of Your Debt and Review Your Financial Position

When you are experiencing a bill-paying crisis, it can be depressing to think about how much or how many people you owe, but it is essential that you take an accurate inventory of your debt. Now is the time to open that stack of bills sitting on the kitchen table and, if you need to, call your creditors to verify your current balances. Once you have up-to-date information, fill out the Debt Worksheet below.

Debt		
Creditor Name	Balance	Monthly Payment
Total		

If you have found ways to increase your income and/or reduce your expenses, you should be in a better position to pay all of your bills. But how do you know if you have done enough? Plug in your income, expenses, and debt payments to the Cash Flow Summary chart, reflecting what changes you think you can realistically make in the near future. (E.g., if you are currently spending \$3,000 a month, but are fairly confident that you can bring it down to \$2,500 a month, list \$2,500.)

Cash Flow Summary	
Total monthly net income	
- Total monthly expenses	-
- Total monthly debt payments	-
= Monthly surplus or shortfall	=

If you have a surplus, you are in good shape. If you have a deficit, look over your budget again and see if there is anything else you can change.

STEP 4: Prioritize Bills and Communicate with Creditors

Changes cannot always be made instantaneously. For example, if you plan to get a second job, it could take a month or two of resume submitting and interviewing before you land one. What should you do in the meantime? Unfortunately, you may have no choice but to pay some bills and not pay others (or pay less than the full amount due). Think about what bills are most important and pay those first. Every person can have a different definition of what is important, but in general, you should prioritize bills which enable you to take care of the essential needs of your family (such as the rent or mortgage, basic utilities, and medical insurance) and for which the penalties for not paying can be severe (such as child support and back taxes).

For any bill that you cannot pay in full or feel you will not be able to pay in the future, you should contact the creditor or service provider immediately. You may be scared that they will be unsympathetic and demand payment – and they may – but many creditors and service providers are willing to work with consumers experiencing hardships. The worst thing to do is do nothing. When communicating, keep in the following tips in mind:

- **Be specific and honest.** Creditors generally like to know what the cause of your hardship was. Be specific and don't lie, even if your hardship is due to something like spending \$15,000 on a Caribbean cruise. True, creditors tend to be more likely to work with customers whose difficulties are due to circumstances beyond their control (like a job loss or illness), but if you are less than honest, they may be less willing to help.
- **Have a plan for the future.** If a creditor feels that you are making little effort to pay your bills, they probably will be hesitant to do anything for you. However, if they know that you are looking for a second job, trying to rent out your spare bedroom, canceling your cable, etc., it will be easier to convince them to provide concessions for a few months.
- **Remain calm and polite.** When you are facing a financial crisis, it is easy to get upset, especially if the person on the other end of the line is unfriendly or unhelpful. However, yelling at a customer service representative won't make the creditor more sympathetic to your cause. In fact, it may have the opposite effect.
- **Don't make promises you can't keep.** It can be tempting to jump at any concessions the creditor is willing to provide, but remember, you may only get one chance at help. It is better to be honest and tell the creditor that you cannot make any payment, or can only pay so much, than to promise to send money you don't have.
- **Keep a record.** Most people prefer to first contact their creditors on the phone. There is nothing wrong with that, but it is a good idea to keep a record of what was discussed. After every conversation, record the time and date you called, who you spoke with, any actions you said you would take, and any promises the creditor made.

- **Be persistent.** As the saying goes, If at first you don't succeed, try, try again. If you call on the phone and the customer service representative says he or she cannot do anything, ask to speak to a supervisor. If that is not effective, send a letter. A sample hardship letter is below/on the next page. (You should send the letter to the address for billing inquiries and concerns, which is not necessarily the same as the payment address.) Ultimately, the creditor may not agree to do anything, but at least you will know that you gave it your best shot.

Sample Hardship Letter

John Consumer
31 5th St
Anytown, CA 99999
Account number 111111111
January 18, 20X0

ABC Credit Company
5 Main St
Central City, DE 17171

Dear ABC Credit Company:

I am writing to inform you that I was recently laid off from my job and am currently unemployed. I am looking for a new job but anticipate that it will take time for me to get one. The amount that I am receiving from unemployment insurance is less than half of my previous salary, and after making a strict budget for my expenses, I find it necessary to seek assistance from my creditors. In place of the regular payment of \$80 per month, I request that you accept payment of \$30 per month for the next three months.

I thank you for your consideration and would appreciate your cooperation during this difficult time. If there are any further changes in my situation, I will notify you of them promptly.

Sincerely,

John Consumer

Handling Different Bills

Mortgage

Maintaining your housing payments should be your first priority. Mortgage delinquency, if not remedied, can ultimately result in the lender foreclosing on your home. (This is true not only for a primary mortgage but also a home equity line or loan.) However, if making your payments is impossible, don't wait to act. The longer you wait, the more difficult it becomes to reach a resolution.

If you are worried about the long-term affordability of your mortgage or are not particularly attached to your house, selling it may make the most sense. But what if you are having difficulties attracting a buyer? If the lender agrees, you may be able to do a deed in lieu of foreclosure (where the house is given back to the lender) or a short sale (where the house is sold for less than the amount owed on the mortgage).

If you do want to stay in the house, refinancing is one way to bring your mortgage current and/or get better terms, but it can be difficult to get a new mortgage if you have a low credit score or little equity in the home. In general, the best thing you can do is contact your lender and make them aware of your situation.

They may allow you to send reduced payments for a specified period of time and pay the remainder later or modify your loan – reducing the interest rate and/or extending the repayment period to lower the monthly payment.

Rent

Maintaining housing payments is no less important for renters. Just as someone who does not pay their mortgage can be foreclosed on, if you do not pay your rent, you can be evicted. If you are unable to make your payments, contact your landlord immediately. He or she may be willing to accept reduced rent for a few months or allow you to make up missed payments over time. Leaving and renting a cheaper place is another option if the rent is not affordable, but if you have a lease, you are responsible for the remaining months' rent. However, the landlord may voluntarily release you from the lease if you explain your hardship. You can also be let off the hook if the landlord finds a suitable replacement tenant.

Car loans

In some states, cars can be repossessed after one missed payment. Repossessed cars are typically sold at auction for very little, and you are responsible for paying the difference between what you owe (plus repossession and storage costs) and what the car is sold for. If you are delinquent on your car payments or think you may become delinquent, you should contact your lender right away. Lenders are sometimes willing to extend loans to cover missed payments or set up repayment plans. Other possible options include refinancing or selling the car. Some people choose to give the car back to the lender instead of waiting for them to take it. This is called a voluntary repossession. You are still responsible for the remaining loan balance (and it can still be reported as a repossession on your credit report), but the lender may be willing to offer a concession or two if you save them the hassle of having to repossess the car themselves.

Utilities

Delinquent utility payments can cause your service to be suspended or terminated, but some utilities are more important than others. You may not be able to live without electricity or water, but you could probably live without cable television. If a service is not needed and cannot be paid, you may want to just cancel it. If a service is needed, call the utility company and ask about payment arrangements –

you may not have to pay the full amount owed right away. You can also see if they (as well as local non-profits) have any payment assistance programs for people facing economic hardship.

Insurance

If you can't make your insurance payments, call your insurer(s). If you allow your insurance to lapse, you may find it difficult to get new coverage or have to pay a large amount to reinstate your policy.

- **Auto:** For auto insurance, see if your insurer can increase the deductible on your collision and comprehensive coverage. This will lower your premiums. If your car is older, you may want to consider going with a liability-coverage-only policy.
- **Life:** It can be tempting to let a life insurance policy lapse, but consider what would happen to your family if you or your spouse died. If you have a cash value policy, you may be able to use some of the cash value to pay your premiums or switch to a term policy (which is usually cheaper). If your policy is “flexible”, you may be able to skip a payment or two. Reducing coverage, instead of canceling the policy completely, may be another possibility. Discuss with your insurance agent what options are available for your policy.
- **Health:** Some people have their health insurance paid for by their employers, but many people don't. The premiums for a standard policy can be astronomical. If your income is below a certain limit or you are pregnant or disabled, you may be able to get coverage through Medicaid or a state health insurance program. Otherwise, if you cannot afford the premiums for a standard policy, you may want to look into catastrophic medical insurance. Catastrophic medical insurance only covers major medical events, like hospital stays, and thus, the premiums tend to be more affordable.

Unsecured debt

There are many types of unsecured debt, including credit cards, personal loans, lines of credit, and store cards. Paying your mortgage or rent is more important than paying your credit card bill, but keep in mind that neglecting unsecured debt, especially if it is done for a long period of time, can result in collection and legal actions, as well as credit report damage. Fortunately, there is often some flexibility with unsecured debt. Many creditors offer hardship

programs – short-term payment arrangements that allow you to make smaller payments. Often creditors will lower the interest rate as well.

Student loans

Borrowers experiencing financial difficulties with student loans can often get a temporary suspension of payments through a forbearance or, less frequently, a deferment. Additionally, some borrowers may qualify for lower payments through an alternative repayment plan, such as the income-sensitive repayment plan. If you are behind, you may be able to become current by consolidating your loans. (Of course, you do not have to be behind to consolidate.) Defaulted borrowers with public student loans also have a one-time right to get out of default with a reasonable and affordable repayment plan. Allowing a student loan to go into default and not doing anything to cure it can result in credit report damage, wage garnishment, and interception of tax refunds.

Child support and alimony

Child support and alimony are not expenses that can easily be reduced. If there is a formal court order in place and you want to have the payment amount modified, you must go back to court, even if your ex-spouse or the child's other parent agrees to the change. It is likely that you will need the assistance of a lawyer or, at the very least, a legal service. Keep in mind that modifications are not retroactive – you are responsible for paying the full amount of all past due payments. Also, you cannot discharge past due support in bankruptcy. Neglecting these obligations can result in very aggressive collection actions, including wage garnishment, tax refund interception, and even jail time (for child support only).

Taxes

The IRS has many methods at their disposal to collect unpaid taxes, including wage garnishment, liens, and seizure of property. However, contrary to what you may believe, the IRS is generally willing to work with taxpayers who want to get back on track. If you haven't filed in years past, do so right away. It is a crime to not file a tax return when you owe taxes. If you cannot pay the amount owed in full, you may be able to set up a monthly repayment plan or establish an offer in compromise (a settlement of the debt for less than amount owed). In cases of extreme hardship, the IRS may be willing to temporarily suspend collection activity. The IRS can be contacted at 800-TAX-1040.

Your Rights

If you are skipping payments on some bills, it is unlikely that those creditors will sit around waiting for you to call them. Many, if not all, will likely call you – a lot – and probably send letters as well. While it is generally in your best interest to communicate with your creditors, you do not need to put up with abuse.

The federal Fair Debt Collection Practices Act (FDCPA) regulates collection agencies' conduct toward consumers. (State law regulates the conduct of creditors' internal collection departments. Many states have adopted the same or broader standards than the FDCPA.) The FDCPA prohibit bill collectors from engaging in the following activities:

- Calling you multiple times a day. They are also not allowed to contact you before 8:00 AM or after 9:00 PM unless you give them explicit permission to do so.
- Contacting you at work if you tell them that your employer disapproves.
- Letting a third party know they are trying to collect a debt from you. However, they are allowed to ask for your contact information.
- Contacting you directly if they know you are represented by an attorney.
- Using false threats, such as saying they will sue you when they have no intention of doing so.
- Using obscenities, racial slurs, or insults.

Additionally, the law gives you the right to stop all communication from a collection agency. You should make the request to cease contact in writing and send your letter certified mail. (A sample cease and desist letter is below/on the next page.) Once the collection agency receives the letter from you, they are only allowed to communicate with you once more to let you know the action they plan to take with the debt. Keep in mind that while sending a cease and desist letter will stop collection calls and letters, it may cause the collection agency to take legal action against you.

If a collection agency violates the FDCPA, you can report them to the Federal Trade Commission at 877-382-4357. Violations committed by internal collection departments can be reported to your state's attorney general's office.

Sample Cease and Desist Letter

John Consumer
31 5th St
Anytown, CA 99999
Account number
222222222
March 13, 20X0

XYZ Collection Agency
211 Grand Ave
Northtown, NV 55555

Dear XYZ Collection Agency:

For approximately three months, I have received multiple phone calls and letters from your company concerning my account. Under the rights granted to me by the Fair Debt Collection Practices Act, 15 USC 1692c(c), I am asking you to cease all forms of communication with me, except for the reasons specifically set forth by federal law. If you fail to comply with this request, I will report your company to the Federal Trade Commission.

Sincerely,

John Consumer

Is Bankruptcy the Answer?

In some situations, bankruptcy can offer welcome relief from the stress of bill problems, but because of the long-term damage to your credit that bankruptcy causes, it should generally only be considered as a last-resort option. While your current employer cannot fire you for filing for bankruptcy, it can make it harder to find new employment. Filing for bankruptcy can also make it harder to rent an apartment, get new credit, or obtain a checking or savings account.

The two most common types of personal bankruptcy are Chapter 7 and Chapter 13. In a Chapter 7, also called a “straight bankruptcy”, your assets are liquidated and used to pay your creditors. If the value of your assets is less than the amount you owe, the remaining debt is discharged (meaning you do not have to pay it). So, if you file for Chapter 7, will they take your favorite sweater and the living room sofa? No. You are allowed to keep, or exempt, some property. (Every state sets its own exemption rules.) If all of your property is exempt, your creditors get nothing. In order to qualify for Chapter 7, you must pass a “means test”. Essentially, if the court feels that you have some money to repay your debts, you will not be allowed to file for Chapter 7.

A Chapter 13 is a court-supervised repayment plan, which typically lasts between three to five years. The court determines what your monthly payment is and how much each creditor gets. Any balances remaining upon the completion of the repayment plan are discharged. You get to keep all of your assets when you file for Chapter 13, even if the value is greater than your state’s exemption amount. You do not need to pass a means test to file for Chapter 13.

Not all debts can be discharged through bankruptcy. Debts that you most likely will still be responsible for include child support, alimony, taxes incurred within the past three years, student loans, and court-ordered damages. Furthermore, you must reaffirm and continue to pay secured debt, like a mortgage or car loan,

if you want to keep the collateral. However, you can include delinquent payments in a Chapter 13 repayment plan.

While it is possible to file for bankruptcy without using an attorney, it is not recommended. An attorney can ensure that all paperwork is filled out correctly and help you determine what type of bankruptcy you qualify for. Your local bar association should be able to refer you to bankruptcy attorneys in your area. If your income is limited, you may qualify for free or low-cost legal assistance.

STEP 5: Rebuild Your Credit and Start Saving

If you cannot pay a bill and are unable to make arrangements with the creditor, it is possible that your credit report and score will suffer. Creditors typically will report delinquencies in excess of 30 days to the credit bureaus. (Utilities and other non-credit bills tend to not get reported until they are sent to a collection agency.) Late payments and most other negative information can stay on your credit report for seven years. You may be thinking to yourself, But I don't want to have bad credit. No one does, but think about where your credit report fits among all of your other priorities. In other words, given a limited income that does not enable you to pay all of your expenses and bills, what is more important: keeping a roof over your head and food in your stomach or having immaculate credit?

Once you have gotten through your financial crisis, you will be in a better position to work on rebuilding your credit. Resume making your payments on time, and keep your balances on revolving debt (e.g. credit cards, lines of credit) low. Time is your friend. Although late payments can stay on your credit report for seven years, the older a delinquent payment is, the less of an effect it has on your credit score, especially if your recent payment history is positive. If all of your accounts were closed, look into opening a new account. With a low credit score, you may need a co-signer to get approved. A secured credit card is another option. Secured credit cards require you to make a deposit, which the creditor gets to keep if you do not make payments, and are usually the easiest type of credit to get.

While we all hope to never encounter financial problems again, the unfortunate truth is that many families face hardships multiple times in the course of their lives. However, even though many problems cannot be prevented, you can at least prepare for them. One of the best ways to prepare for a financial crisis is to have emergency savings – most financial experts recommend that you set aside at least three to six months worth of essential living expenses. If your account is currently running on empty, saving that amount of money may seem like an impossible task, but it is not. Once your financial situation stabilizes, start setting aside whatever you can, be it \$30 a month or \$100. Make it an automatic process by having some of your paycheck directly deposited into your savings account or setting up a weekly or monthly automatic transfer from your checking account to your savings account. Pretty soon, you will find yourself with a tidy sum, and if another financial storm comes your way, you'll be covered.