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## How To: Tackle Your Debt in Five Simple Steps

by [Cap](#) on 5/16/2007

Tags: [Finance Core](#), [moneyhacks](#)

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Any Mint reader who finds themselves stuck under a mountain of consumer or credit card debt understands the anxiety involved with owing money. Over [half](#) of American families with credit cards report having at least some debt, so what can you do to lift that weight off your shoulders?

You may be surprise to hear this, but axing that debt is actually a very simple thing to do (it's just not always *easy*).

### Step #1 - Spend Less Money Than You Earn

This sounds trivial, but step number one in getting out of debt is pure mental discipline to spend less money than you earn. The minute your income exceeds your expenses is the minute you have money left over to pay towards your financial debt. It's surprisingly easy to neglect, so don't make the mistake of

overlooking a month here and there or “just letting that last bill slide.” Taking charge of your debt means taking charge of your spending life.

**Simple example:** You make \$1,000. You spend only \$500. You now have \$500 left to apply towards your debt.

Once you master the discipline to spend less than you earn, you’ll find that the rest of the steps are easy in comparison!

## Step #2 - Distinguish Between Bad Debt & “Okay” Debt

An okay debt has an interest rate well under 10%, which generally means around 3-6%. Mortgages and student loans are examples of an okay debt. Auto loans are a bit on the borderline, because even though auto loans have fairly low interest rate, the car’s value will depreciate quickly.

What would be a bad debt?

Everything else! Your platinum credit card at 16%, 19%, 21% interest rate, for one, and your financed furniture or television for another.

Now that you have distinguished between bad debt and okay debt, it’s time to do something about the bad debts!

## Step #3 - Pay More than the Minimum

Gather up all the bad debt, your credit card, bill statements and line them all up. Add up all the minimum payments for the amounts owed and pledge to pay the overall minimum and an extra chunk to one single account. Important note: If you don’t pay more than the minimum payment, you will not be able to get rid of these debts within a reasonable time frame.

**Extreme Example:** Let’s say you have \$8,000 in credit card debt on an account with 16% APR and your minimum payment is 2.5% of the balance (\$200 for a balance of \$8,000). If you only pay the minimum payment base on balance, it would take you over 26 years to pay off your balance! During this time frame, you would pay over \$8,800 in interest!

What happens if you apply a fixed payment of \$300 to the balance every month instead? It would take you about 3 years to pay off the balance, and it would only cost you about \$2,000 in interest. Definitely quite a difference.

## Step #4 - Tackling the Worse Among the Bad Debt

From your lined up bills, find from your statement the interest rates for each of these accounts.

**Example:** You may have \$2,000 at 13% APR; \$6,000 at 16%; \$3,000 at 19%; and \$400 at 14%.

Put the extra chunk toward the highest rated debt first, which is the \$3,000 account at 19%. If you wish, you can also start off by paying any low amount accounts, such as the \$400 account — even if its interest rates are lower. Doing this will get one account out of the way, and it would be a good boost to your confidence in getting rid of your debt.

Continue to pay the minimum payment for the rest of the accounts, and apply the extra chunk to the highest interest rate account. Keep going at it month to month; once you're done paying off one account, head towards the next highest interest rate account. Rinse and repeat until the very last bad debt goes bye-bye!

### Step #5 - Ask For a Lower Rate

As you are paying off the debt on your various accounts, take a moment to do this one final step: ask for a lower rate! Look for any account over 14% in interest rate, and call that company to ask them to lower your interest rate to 11-12% (or even lower if possible).

Tell them that you have received offers from other companies for a much lower rate, and that out of simplicity (or loyalty) you want to stay with them. This might not be a very fun thing to do, and you may feel uncomfortable in asking for a reduction in your rates, but you may be surprised to find that many credit card companies will be willing to lower your rates if you just ask.

Remember this, you are a source of revenue for these companies; at the end, most of them would rather lower your rate than lose you as a customer. Don't be afraid to close your account and transfer your balances if you can't get the rates reduced.

**Related Resources:** [Tips to balance transfer correctly!](#)

### Getting Rid of Your Debt Check-List

1. Spend less money than you make.
2. Differentiate between bad and okay debt.
3. Pay more than the minimum.
4. Pay the highest interest rate debt first, and then tackle the second highest rate debt and so forth.
5. Ask for a lower rate to current high interest rate debt!

The concepts to paying off your debt are simple, but it certainly isn't an easy thing to do. It takes discipline, consistency, and patience to pay off your debt — and although it isn't easy to get out of debt, it also isn't impossible.

You will find that many people have also faced the challenge of paying off their debt. The ones that succeed in eliminating their debt are the ones that persevere under the challenge.

And that's the key point, to keep at it! To consistently spend less than you make, pay more than the minimum, and before you know it, you will be well on your way to becoming debt free.

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Eric Says:

[May 16th, 2007 at 12:56 pm](#)

In example 4, you will also benefit by paying off the higher interest debts with the lowest interest one. From the example:

You may have \$2,000 at 13% APR; \$6,000 at 16%; \$3,000 at 19%; and \$400 at 14%.

You can use the 13% credit vehicle to pay off the other 9400 (if possible) and consolidate all the debts to 1 lowest interest payment. Then go back to #3.

[Moneymonk](#) Says:

[May 16th, 2007 at 4:17 pm](#)

you misspelled Gather under step 3

I have good debt ( house, student loans) both under 10%. I carry no consumer debt. Although I am not behind on either debt. I have to execute #3 Pay more than the minimum

That one move can save you a lot of money and plenty of time

Thermopyle Says:

[May 16th, 2007 at 4:45 pm](#)

I'm with Dave Ramsey on the notion that for most people under most circumstances paying off the smallest debt first and progressing up the debts in size order reaps psychological benefits which will help you keep disciplined in paying off the debt.

[Cap](#) Says:

[May 16th, 2007 at 5:03 pm](#)

Eric: That's a great point Eric, consolidate other accounts into a lower rate account when possible and without fees would be a good way to reduce amounts you pay via interest, and make it easier to keep track of your payments too. Thanks for adding that in.

Moneymonk: Doh! Not sure why spellcheck didn't catch that typo but I suppose I can say the same about why I didn't notice it during proofing.

Paying more than the minimum can definitely save you a lot of money in the long term, but if the home or student loan is of low enough interest rate, it may not be a bad idea to contribute your money to other funds such as retirement accounts. After all, there's no such thing as a retirement loan when you're old!

Thermopyle: Hmm that may be true, I can see how that will help in building discipline, but I also believe that many people can also develop discipline even if they're paying higher amount accounts. In certain circumstances, tackling debts w/ the highest rate first will save staggering amounts of money!

Of course, as Eric suggested... you can simply consolidate or transfer all funds into a single account, and that'll throw that problem out of the window 😊

[modemlooper](#) Says:

[September 9th, 2007 at 8:41 pm](#)

If you are current on student loan payments then defer them and use the money you would pay them off to credit card debt.

Jason Says:

[October 24th, 2007 at 1:07 pm](#)

Another good tool for paying off consumer debt is prosper.com. I consolidated several loans under one payment with a lower interest rate than any of the credit cards had (and 2% lower than anything banks would give me). I'll be bad debt-free for the first time in 4 years with my December payment. 100% recommended.

Also, having a product that aggregates all your financial information (currently I use yodlee's moneycenter, but I'm evaluating mint - they need to handle investments before I switch) is a huge motivational helper. Watching your net worth go up really helps. Now, when presented with a large chunk of money (yearly bonus, tax return) I'm more likely to put it in savings instead of buying some new gadget - just so I can see my net worth go up. And in December, I'll be in the black again, and I'm throwing a party to celebrate.

[How To Get Rid Of \\$35 000 In Debt « USMLEMD](#) Says:

[December 5th, 2007 at 12:47 pm](#)

[...] [How To: Tackle Your Debt in Five Simple Steps \[mint\]](#) Photo by [quaziefoto](#) [...]

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