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## Chapter 1- The Decision to Borrow

### Background

The wealth creation journey of individual is rife with may financial decision-making situations and some of the most important decisions one has to make are about borrowing, the decisions could involve

1. Whether or not to borrow
2. If I am borrowing what are the rates at which I should borrow
3. Should I take on new credit cards
4. How to get out of a financial stress situation caused by debt

As a financial advisor/planner you must be coming across clients who are facing any such situation and, in these circumstances, a financial advisor has to assume the role of a debt advisor.

This program focuses the parameters and factors that you need to consider while making the decision regarding debt in your life.

### The decision to borrow or not borrow, what kind of assets to borrow on is an important decision but equally important is the availability of credit, i.e. when you decide to borrow, the credit facility should be available to you.

### Debt

As per “Investopedia”

Debt is something, usually money, borrowed by one party from another. Debt is usually taken by individuals and corporations to make purchases that they won’t be able to do in the normal circumstances under their current sources of income

A Debt agreement gives the borrowing party the permission to borrow the money under the condition that it is to be paid back at a later date usually with interest

Debt: - Debt is borrowing and in financial sense, we are talking about the borrowed money, the money that is borrowed has to be repaid, mostly with an interest.

In the modern times, as we can see borrowing comes in many forms,

1. Loans
2. Credit Cards
3. Buy now pay later
4. Other forms of borrowing

## The Role of Debt

Debt can play a variety of roles in your financial life, but if you look at the broad level there are mainly two purposes

1. **To Create Assets**
2. **To fund deficit in Expenses**

When, as an individual one looks to purchase an asset,, which is difficult to purchase because on one time cash outlay, one may borrow to buy the asset.

This decision can lead to wealth creation or wealth erosion in long term, depending upon the nature of asset that has been purchased using the asset

Assets Can be classified into

1. **Appreciable Asset**
2. **Depreciable Assets**

Appreciable assets are the assets that gain value in the long term, while depreciable assets are going to reduce value in the long term, Example of appreciable assets will include

1. **House**
2. **Mutual fund investments**
3. **Fixed Deposits with banks**

Appreciable assets are also known as Capital assets, and the value gained by thee assets are known as capital gains

Examples of Depreciating assets will include

1. **Car**
2. **Mobile Phone**
3. **Air-conditioner**

Depreciating assets are known as use assets, and they keep on losing value until they reach the end of their useful life, at which time, the value remaining in the asset is known as salvage value.

## Is Borrowing always wrong

The general perception and connotation attached with borrowing has been negative, traditionally it is not considered good to borrow, but can we say plainly that borrowing is bad

The answer to above question is no, borrowing is not always bad, in certain cases, borrowing may help increase your net worth and thus contribute in wealth creation.

Debt can be utilized by individuals for two purposes

1. For asset creation
2. For Expenses

The utilization of debt is better for asset creation than expense, if you are utilizing debt for funding your expenses, then it will become very difficult to create asset of any kind.

Even while taking debt for creating asset, it will contribute in wealth creation only if the asset is appreciable in nature,

Acquiring an asset using debt creates an asset along with a liability in terms of loan, over a period of time, with repayment the value of liability will decrease and if the value of the asset increases during this time, then the net contribution to the net worth is positive.

But in case of a depreciable asset, if the value of the asset in question falls faster than the liability then the net contribution in the net worth is negative and the decision may result in wealth erosion

## Points to remember

1. Borrowing is not always bad, in some cases borrowing can help you create wealth
2. You must do a proper analysis, of the purpose for which the debt is going to be utilized
3. Assuming debt is preferable, when the asset in question Is appreciable in nature
4. Avoid taking debt for depreciating asset, even if you have to take debt then keep the term as minimum

**A graphical illustration of the impact of a housing loan on the net worth**

## Types of Debt

* Secured Debt- Taken against an asset as Collateral

-Property loan- Against Property of the Borrower

- Car Loan- Car acts as Collateral

- Gold Loan- Gold is kept as collateral

* Unsecured Debt- Without any Security/ Collateral

- Personal Loans

- Student Loans/ Education Loan

* Revolving Debt- Line of Credit- Credit Card
* Mortgages

- To buy homes, or a large asset and to be amortized over a long period of time

## Kinds of Debt

* Housing Loan- Secured
* Car Loan- Secured
* Loan on Consumer Products- Unsecured
* Education Loan- Unsecured
* Personal Loan- Unsecured
* Credit Card Debt- Unsecured
* Buy Now Pay Later- Unsecured
* Bank Overdraft Facility-Unsecured
* Cash Credit Limit- Unsecured
* Revolving Credit Facility- Unsecured

## Discretionary Vs Indiscretionary Expenditure

If you are utilising debt for taking care of your Indiscretionary expenditures, then you need to have a look at your budgeting, this is a situation of deficit, which if continued for a long time may bring a lot of financial stress in your life.

For Discretionary expenditure the following quote of Warren Buffet may Suffice

“If ***you buy things that you don’t need, then you will soon have to sell the things that you need***”

Discretionary Expenditure could be eating out, online shopping, and other such things

One should be very careful about utilising debt

Thus, at the end we can say that debt can either help you in creating assets or it can help you manager your day-to-day expenses and hence a proper analysis is warranted when one has to make a decision whether to acquire debt or not.

## Conclusion

* Borrowing is not always bad, In certain cases borrowing may lead you to trouble, however in other cases borrowing may indeed result in an increment in your wealth
* One thing that has to be strictly followed while borrowing is that the repayment has to be within time
* Borrowing should be avoided for the items that are depreciating in nature
* One should not borrow for the things which have no salvage value
* If you have to borrow, borrow for acquiring the assets that appreciate
* The eye must be on the net worth
* The decision to Borrow must have a positive impact on the net worth

## Chapter 2- Debt Advisory

Debt advisory or credit counselling is a specialized service offered by financial advisors and planners in which they help their clients use debt more effectively for the purpose of wealth creation and avoid debt traps. It also helps in using the credit judiciously towards ensuring the financial well-being.

Following services can be considered a part of Debt Advisory,

Helping the client in

1. **Raising finance to acquire new property: -** The advisor will help the client identify the best source of debt, finalizing borrowing terms including interest rates, Loan term, and the quantum of Borrowing
2. **Raising finance to support growth**: Sometimes the client needs fund to expand the business, or buy some new assets that will support the growth of the business and thus revenue, a debt advisor helps the client in identifying the right source and will assist in getting the disbursal in time
3. **Using Equity to settle debt**: This is a specific example in which a debt advisor can help the client in negotiating new terms with the lender in case of a financial stress situation, i.e., when a client is not able to repay the debt the advisor can help the bank to agree on reducing the amount of mortgage in exchange for equity when the asset is sold
4. **Refinancing existing debt facilities or securing new debt product**: Sometimes the client gets into financial stressful situation because of wrong decision making and assuming of debt without proper analysis of available resources and repayment capacity, under such situations, the adviser can create strategies, that will help the client come out of the stressful situation
5. Realizing Value through Debt Restructuring: A very important aspect of the work of a debt advisor is debt restructuring, deb restricting means altering the structure of debt in a manner consistent to the payment capacity of the client, there are several strategies to this that has been discussed in detail in the final chapter
6. General advice to come out of financial stress full situations

To provide these services, as a financial advisor you must be able to analyze and understand these situations and provide sound advice so that the wealth creation process is not interrupted.

A personal finance customer will require advice at a time of

1. Getting a large mortgage, housing education loan etc
2. How to utilize revolving credit facility like credit card
3. Whether to prepay a loan or not
4. To steer out of financially stress full situation
5. How to maintain good credit profile and good credit history
6. When it is right to borrow

Often the professionals that offer Debt Advisory as a service, only involve themselves in the introductory stage of a lending transaction. For example, a finance broker or financial advisor may only refer the borrowing request to their pool of trusted lenders, leaving the co-ordination of their request to the client.

However, a Debt Advisory service should be much more than this. It is about supporting the client through every element of their borrowing request from start to finish.

This begins with understanding the clients, their business and personal goals. Once this is established then the advisor can search for appropriate funders, obtain deal structure and pricing indications, gain credit approval, co-ordinate professionals, eg lawyers, accountants, valuers and contractors, and arrange the discharge of lending conditions and covenants to enable draw-down and completion.

A debt advisor will co-ordinate every element of the transaction to relieve the stress, time and burden from the client.

## CHAPTER 3-LOAN AMORTIZATION

When you take a loan, it is repaid in equal installments. Most of the loans given to individuals by banks and financial institutions are in the form of reducing balances loans. With Each repayment (EMI) some part of the interest and some part of the principal is repaid, the interest charged by the bank for each period is on the remaining amount of principal balance that is remaining after the payment of last EMI.

## Loan Amortization Schedule

* A loan amortization schedule is a schedule of the EMIs bifurcated into interest and Principal
* Since most loans are given on reducing balances, a detailed amortization schedule will help us in understanding the interest and the principal
* While there are templates of amortization schedule, an most of the times banks get a printout of the amortization schedule from the bank
* Making an amortization schedule yourself on excel, will give you a better understanding of the loan dynamics, understanding the movement of principal and interest
* This will be useful in making a decision on loan pre-payment, vs EMI reduction in case of a loan refinancing situation

## Financial Functions of Excel

To make loan amortization schedule you should know the financial functions of excel, more specifically time value money functions of excel. In our live session we have covered detail how to use these functions

Following five functions will help you in calculating the related values and make a loan amortization schedule

1. **FV (Future Value)-** It Calculates the value of the current investments as at the end of the investing period
2. **PV (Present value)-** It Calculated the value as on today
3. **PMT-**The function calculates equated payments (EMI of a Loan or SIP)
4. **NPER-** The function calculates the term required to achieve the goal
5. **Rate:** - Calculates the Rate of Return

You can use a time line to decide which function to use while making financial calculations

**Time Line**

**0 1 2 3 4**

Tick marks occur at the end of the period, and you can make the decision about the function to be used as per the timeline

If the value to be calculated is at the time 0, you have to use PV

If the Value to be calculated is at the end of the timeline use FV

If the Value to be calculated is at each tick (Equal Value) use PMT

If you want to calculate the number of ticks, use NPER

If you want to calculate loan rate, you may use RATE

## For a loan Scenario

1. PV=Loan Value
2. FV=0
3. NPER= Loan Term
4. Rate= Rate of Interest
5. PMT= EMI (to be calculated)

To access these functions, you may go to the function tab in Excel and select financial functions in categories.

**Path**

Functions- Financial- FV/PV/PMT/NPER/RATE

**Loan EMI**

To calculate the EMI of a loan, the PMT function in Excel has to be utilized with the, each of the above-mentioned function will require the other four values in order of main value to be calculated.

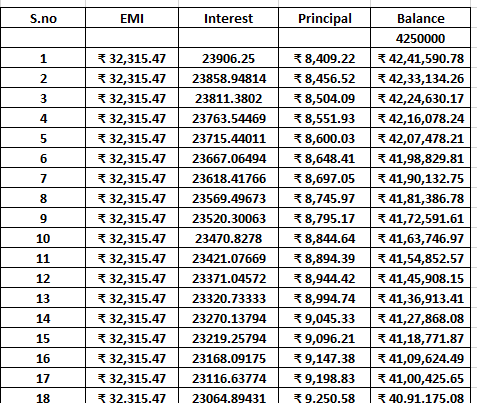


Figure 2.1: A loan amortization schedule

For the complete schedule in Microsoft excel, you may refer to the excel sheet provided

## Chapter 4- Debt Trap

Debt Trap is a situation when an individual has acquired more debt than his repayment capacity will permit, some characteristics of Debt Trap are

1. The interest outgoing is more than the repayment capacity
2. You are paying only a minimum amount, and the amount keeps ballooning
3. Debt has been taken indiscriminately without giving a thought to repayment capacity
4. You have utilised the credit limit of the credit facility in a onetime expense or emergency and are struggling to come out of debt

Managing your finances is very crucial to financial wellness of an individual, despite that many people find themselves in unfortunate situations as debt trap, following are some of the mistakes that can lead people to debt trap

**What Causes Debt Trap?**

* It’s very important that you identify the reasons that could cause you to fall into a debt trap. They include
* Your EMIs exceed 50% of your income
* Your fixed expenses are more than 70% of your income
* You have exhausted your credit card limit
* You have too many loans
* You cannot afford to put aside money for savings
* Your loan application is rejected

**Your EMIs exceed 50% of your income**

With easy finance available, a lot of people have become compulsive spenders. They easily fall prey to discounts, sales, etc. and end up buying things on EMIs. These EMIs on their own may not be a big amount, but when added, they can be a significant amount, leaving less money to spend on other important things.

If you see your total EMI amount exceed 50% of your income, it’s a red flag – you could be on your way to becoming a victim of a debt trap.

**Your fixed expenses are more than 70% of your income**

EMI is not the only financial obligation; there are other fixed expenses you need to take care of every month. These expenses include rent, school fees, electricity bills, etc. Ideally, your fixed financial obligations-to-income ratio should not be more than 50%; if it exceeds 70% of your income, it’s a warning sign that you are slowly getting caught in a debt trap. Experts insist that you need at least 30% of your income for other expenses and to meet your financial goals.

**You have exhausted your credit card limit**

It’s so easy to purchase goods by swiping your credit card – buy what you want without worrying about paying for it upfront. But, if you find yourself in a situation where you’ve maxed out your credit card limits, it’s time to take a pause and rethink your financial standing – you could be in a debt trap.

**You have too many loans**

If you are repaying too many loans at different times of the month, it can be not only exhausting, but also you may be putting yourself at risk of defaulting. Additionally, you may be losing a lot of money by paying interest on so many loans.

**You cannot afford to put aside money for savings**

If you are not able to save money every month, it could be because of your debt and other fixed expenses. This is yet another sign of getting into a debt trap.

**Your loan application is rejected**

If your loan application has been rejected, then it’s the ultimate sign that you are in a debt trap. Before approving a loan, banks and financial institutions check your credit report to assess your creditworthiness. If you are knee-deep in debt with no financial capability to pull off another loan, banks will not extend you with more credit. Even if they do, it will be at a much higher interest rate which can push you into the vicious cycle of debt with less or no hope of return.

**How to Come Out of the Debt Trap**

**Determine the problem and analyse it**

A detailed and meticulous review can provide you with the answer to your existing debt situation.

Here’s what you can do:

* Firstly, you need to acknowledge and admit that you have a debt problem.
* Identify areas that are causing you to fall into a debt trap.
* Create a plan to work on these areas.
* Make a budget and prioritise your needs

**Make a budget and prioritise your needs**

After a thorough analysis of your debt situation, you may now be able to identify essential, semi-essential and non-essential expenses.

* Create a priority list of all your needs.
* Make debt repayment your first priority, as that can have a positive and long-term effect on your financial situation.
* Refrain from indulging in non-essential or even semi-essential items at least till you are back on track.

**Opt for a debt consolidation loan**

Instead of repaying different loans at different times in a month, you could consider consolidating your high-interest debt by getting a [low-interest personal loan](https://www.moneytap.com/personal-loan.html) or a [debt consolidation loan](https://www.moneytap.com/debt-consolidation-loan.html). After debt consolidation, you just need to worry about making one payment to one lender every month.

By doing so

* You save money on interest,
* You pay your EMIs on time,
* Your debt gets paid off faster, and
* You regain your financial vigour

**Automate the payments**

Repaying your loan in EMIs is the financial commitment you make with your lender. Automating your payments can ensure that you do not break this promise. The benefits of setting up an ECS mandate with your bank to automate repayments have the following benefits:

* You regularly pay on time.
* Timely payments reduce your debt faster as you save on interest, late fees and penalties.
* Your credit score gets a boost.

**Avoid taking on more debt**

While you’ve already borrowed to the hilt, avoid borrowing more. Make it a rule to keep your debt-to-income ratio, not more than 40%. Otherwise, you’ll be straining your finances so much that you’ll be setting yourself up for a financial disaster if you happen to lose your income for whatever reason.

**Look for ways to increase your income**

One of the ways to get out of debt is to increase your income. The extra income can be used to pay off your debt faster. Pick up freelance gigs or a second (part-time) job that’s relevant to your skills, knowledge and experience.

**Pay off the expensive loans first**

If you are not considering debt consolidation and want to pay your debts separately (tackling one debt at a time), create a plan to pay off the most expensive loan first.

**Check your credit score frequently**

A [healthy credit score](https://moneytap.com/blog/how-much-is-a-good-credit-score/) is the hallmark of a good borrower. If you have a score of 750 and above, you attract the best of lenders, best of interest rates and best of loan terms. So, if you want to enjoy a healthy financial future, you need to keep a tab on your credit score. Make it a point to request your credit report at least once in 3 months or after the closure of a loan account. Check whether the details recorded are correct and as per your expectations.

**Get professional help**

If you find it difficult or almost impossible to get out of the debt trap on your own, it is best to consult an expert. Financial professionals can offer you counselling on your budget and impose spending limits. Some professionals may even negotiate with the lender on your behalf to make the loan terms more favourable for you.

**Debt Consolidation – A Clever Solution to Come Out of Your Debt Trap!**

Debt consolidation is one of the best ways to make your financial situation healthy. If you carry around multiple high-interest loans or outstanding credit card balances, you are slowly stirring a recipe for a financial mess. Taking a low-interest personal loan is a very clever step to be debt-free. The personal loan helps clear all your outstanding balances and convert your multiple payments into a single monthly payment made towards your debt consolidation personal loan.

**Why taking a debt consolidation loan makes sense?**

* A debt consolidation loan allows you to lower your interest rate, reduce your monthly payments, and pay off your debt quicker.
* It enhances your financial freedom and helps you to budget your monthly expenses properly.
* Since you need to make just a single monthly payment rather than multiple loan EMIs, you reduce or eliminate the chances of missing payments, thus avoiding late fees and higher interest rates.
* It ensures timely payments that improve your credit score and enhance your creditworthiness for future loans.

## Chapter 5- Credit

## Credit Profile

A credit profile is a document which provides information about someone's credit history. Credit profiles are used by lenders and other agencies which offer credit to determine someone's creditworthiness, and they are also utilized by prospective landlords and other people who might have an interest in someone's credit history.

[Good credit](https://www.wisegeek.com/what-are-the-advantages-of-having-good-credit.htm) will make it easier for someone to access credit, while bad credit can become a major stumbling block.

Late or incomplete payments can negatively affect a person's credit profile.

The profile includes a complete history of the credit accounts someone has open or has held in the past, along with information about their limits, the balances carried on them, and the person's payment history. The maximum ever carried on each account will be listed, as will information about late or incomplete payments. Old accounts are eventually dropped from a credit profile after a set number of years, classically seven.

A credit profile includes a complete history of the credit accounts someone has open or has held in the past.

A credit profile also often includes information about someone's employment history, along with listings of any inquiries made about someone's credit. If, for example, someone takes out a loan to buy a car, the inquiry from the lender will show up on his or her credit report, and another lender will be able to see that an inquiry was made. The inquiry history may be used to determine whether or not credit was granted to someone, or to alert the person reviewing the report to the fact that a new credit account may be in the process of being opened.

Credit profiles contain other information, such as employment history, in addition to credit history details.

Credit profiles can be found for individuals and businesses. People who are just starting businesses should take steps to create a separate business profile. This ensures that personal credit black marks will not count against the business, and it can generate access to business loans and other types of accounts which are only open to businesses, not to individuals. Both business and personal profiles should be regularly review for errors, and if errors are identified, a request for correction should be filed.

The best way to build up a credit profile is to keep current on all credit accounts, making payments on time and in the amounts required, or in excess of the minimum. It is also a good idea to avoid carrying a balance in excess of 50% of someone's available credit on a revolving credit account, and to avoid opening too many revolving credit accounts, as this can make someone look like a credit risk. Consumers should be aware that agencies which claim to “fix” someone's credit are often highly questionable, as usually activities which alter a credit report can only be undertaken by the person whom the profile concerns.

## The Importance of Credit Profile

Whether you want to take debt at this point or not, but it is important that debt is available to you when you need it, this will debt on your creditworthiness.

Banks, financial institutions and other bodies check your credit worthiness by accessing the credit reports provided by the credit bureaus, these are some of the credit bureaus operating in India

## Credit Bureaus in India

Risk assessment is one of the most important aspects of human beings. Whatever we do, we analyze the situation to see how much risk is involved in it. This assessment grows even more when we talk about money. In the case of lending money, this assessment gains primary importance. Whenever one wishes to borrow money from a financial institution, they have either have to provide some sort of security or prove their creditworthiness. In cases of unsecured credit like personal loans and credit cards, an applicant has to have a good credit history. The basic test for a person’s creditworthiness is their credit score which is calculated on the basis of a person’s financial history, the credit mix that they have, how they have been utilizing the credit that was granted to them previously and how diligent they have been with repaying their past dues.

Credit scores are calculated by agencies known as credit bureaus. They acquire and maintain a record of every individual’s credit details and helps lenders to understand how worthy an applicant is. This information is collected from data providers. These providers include creditors, debtors, and debt collection agencies etc. Thus lenders can understand how likely a person is for default and who they should grant credit to. The major credit bureaus in India are as follows-

## The TransUnion CIBIL

The TransUnion CIBIL or simply CIBIL is one of the commonly known credit bureaus in India. It was initially known as the Credit Information Bureau (India) Limited. It was established in the year 2000 and is the first Credit Information Company of India to have an immensely strong and wide member base. The credit score issued by this credit bureau is well known as CIBIL score. Approximately 950 entities that include both banking and non-banking financial organizations from both private and public sector, house-finance companies, and other financial institutions are making use of CIBIL score to judge applicants. You can get one free CIBIL score in a year.

## Experian

The complete name of Experian is Experian Credit Information Company of India Private Ltd. It is a commercial financial institution which came into being in the year 2006. Numerous companies including GUS Holdings BV(Netherlands), Union Bank of India (UBI), Axis Bank Limited, Indian Bank, Federal Bank Limited, Punjab National Bank (PNB), Sundaram Finance Limited, Magna Fincorp Limited, and VIC Enterprises Private Limited collectively operate this credit bureau. Experian became the first financial institution to receive the license under the new Credit Information Companies (Regulation) Act (CICRA) 2005 in the year 2010. According to the 2014 editions of the Forbes magazine, Experian is a part of the list of the ‘World’s most innovative companies’ in the world. Both comprehensive and detailed credit report is offered by this credit bureau. The range of the Experian credit score is from 330 to 830. You can get one free Experian score every year.

## Highmark

Another popular credit bureau in India is the Highmark or High Mark Credit Information Services. It maintains a record of credit information for every individual and organization. It was established in the year 2005 and is situated in Mumbai. Apart from collecting and maintaining credit information, this credit bureau also offers credit reports and score to consumers. It enables lenders to access the creditworthiness of an applicant before they approve their credit or loan applications.

## Equifax

Established in Atlanta, USA, in 1899, Equifax was registered as a credit bureau in India by the Reserve Bank of India in the year 2010. It is headquartered in the USA and is amongst one of the largest credit agencies in the country. Equifax also maintains a record of credit information of individuals. It also keeps a track of credit information for all sizes of organizations.

The usage of a credit report does not end at proving your creditworthiness. You can get low interest rates on personal loans and best offers on credit cards if you have a good credit score. Also, one must note that when you check your credit score yourself, it does not have a negative impact on your credit score. One must frequently check their credit report in order to keep a track of their financial progress and also to identify identity theft at the earliest.

## Credit Profile

The credit profile of an individual is the sum of credit history and credit behaviour

* Credit History consists of all the past loan accounts that you have maintained, your credit cards, your repayments
* Credit Behavior looks at the way you treat the credit, how you utilize your credit limits, how you pay off your debts, what percentage of your payments are on time – All these factors contribute towards Credit Profile

Following Information is available in the credit report

1. **Personal Details**

**Each of your credit reports will contain the following basic pieces of biographical information:**

* Name
* Date of Birth (DOB)
* Current & Past Addresses
* Name of Current & Past Employers
* Social Security Number (SSN)

1. **Credit History**

**Your credit reports contain the following information for each account that you’ve opened with a credit card company, bank, or other creditor in the last few years.**

* Date of account opening (and closing, if applicable)
* Credit limit (or loan amount)
* Monthly balance as of each statement date (contrary to what many people believe, credit reports do not list information about individual purchases or other transactions.)
* Monthly payment history that indicates whether or not minimum payments were made on time (credit reports do not list your exact payment amount)

1. **Credit Enquiries**

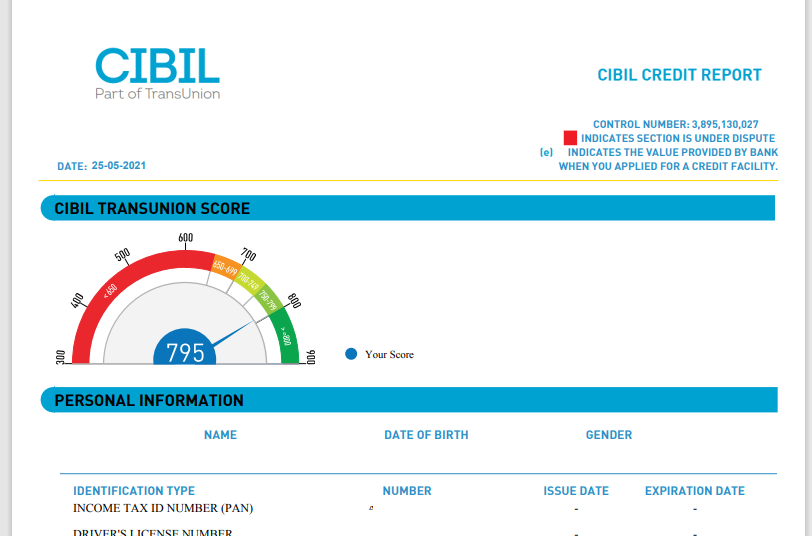
An inquiry is recorded whenever your credit report is “pulled” (i.e. viewed) by another party, such as a lender, credit card company, service provider, landlord, or insurer. Credit inquiries remain on your credit report for up to 2 years, and each can temporarily result in a slight dip in your overall credit standing.

1. **Public Records**

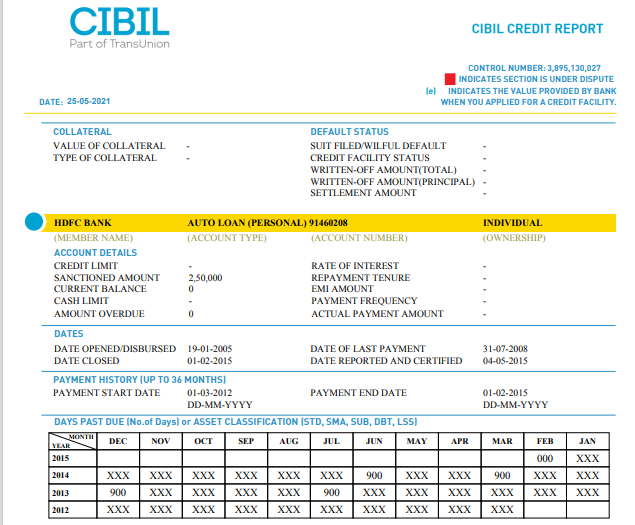
**There are three main types of public records that can be included in credit reports.  Each has a detrimental impact on your credit standing and may remain for up to 10 years.**

* *Bankruptcies:*  Bankruptcies can be listed on your credit reports.  The length of time they will remain there and the damage done to your credit standing depends on the type of bankruptcy in question and whether or not you adhere to the terms of the bankruptcy.  
  But other than that, “there is no way to mediate how much a bankruptcy affects your credit score. It is what it is, regardless of the chapter filed,” according to ***Dr. Deborah Thorne***, an associate professor of finance at ***Ohio University***.
* *Tax Liens:*Courts often attach a notice known as a lien to property records in order to block the sale of the property until unpaid debts (e.g. unpaid taxes) are addressed.
* *Civil Judgments:*If a court finds that you owe another party money (e.g. child support), this will be reflected on your credit report.

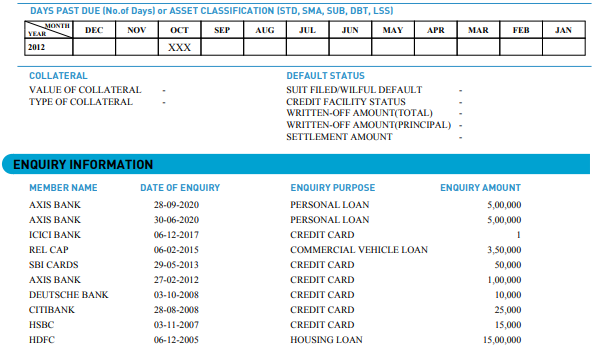
1. Personal Statements



**Credit Report Front Page**

****

**A Loan account being reported in a credit report**

****

**Credit Enquiries in a Credit Report**

## How to maintain a good Credit History

Here are some of the tips to maintain a good credit history

## Pay Complete Bills on Time:

One of the best ways to maintain a healthy credit report is to inculcate self-discipline in terms of prompt payment of your credit card dues. You should always pay your credit card balance in full, as, revolving the credit to next month always attract additional cost and it may become difficult for you to manage this debt at some point of time. Paying your credit card dues regularly helps in boosting your credit score whereas a delay in payment shows up in your credit report as DPD (Delay in Payment Days) and is generally viewed negatively by the lenders. A credit score is dependent on several factors, classifying the repayment history as the most crucial factor. So, if you regularly make payment of all your credit card dues and EMIs on your loan, it definitely improves your credit score over time whereas a delay in payment negatively affects your credit score as well as your credit history.

## Don’t fully utilize your credit limit:

You should avoid reaching the maximum credit limit on your [credit card](https://www.bankbazaar.com/credit-card.html?WT.mc_id=BLOG|ahow-maintain-good-credit-history|TX&utm_source=BLOG&utm_medium=social&utm_campaign=ahow-maintain-good-credit-history_TX). The more you use your limit, the negative it is for your credit score. Although there is no thumb rule, but still most Financial Experts believe that it is safe to use up to 50% of the sanctioned limit on your credit card. For example: If you have a credit limit of Rs. 1,00,000, then your monthly credit card statement balance should not exceed Rs.50,000. Remember, whenever you use your credit card, you are borrowing money from a credit card company. So, using a lesser credit limit implies that you are financially secure and are not reliant on borrowings.

## Keep a Healthy mix of Credit:

Ideally, a borrower should have a mixture of credit in terms of both secured as well as unsecured loans. Secured borrowings include loans like Home Loan, Car loan etc. whereas unsecured borrowings include Personal Loan, Credit Card etc. Most of the loan providers believe that a borrower’s risk of default increases if he/ she is exposed to more number of unsecured loans. Whereas, they feel more assured to lend secured loans. This is another reason why unsecured loans are more expensive than secured loans. Moreover, having different kinds of accounts (i.e., loans) is favourable because it shows that you have experience managing a mix of credit. The ideal credit history should contain a mix of a home loan, car loan and a couple of credit cards.

## Monitor all your accounts regularly:

You should keep a check on all your repayments and ensure time payment for all the loans as well as credit cards wherein you were an applicant, a co-applicant or a Guarantor. A default in a loan wherein you were a guarantor, can equally ruin your credit history as that of an applicant. As a guarantor or co-applicant, you are held equally liable for missed payments. This is extremely important because your joint holder’s negligence could affect your ability to access credit when you need it.

## Review your credit report:

Your credit card providers always share details of your repayment with several credit agencies like CIBIL TransUnion, Equifax etc. who in turn rate you on a credit score ranging from 300-900. It is a good practice to buy your credit score and complete report, at least once in a year to keep track of your credit history. Your credit score tells the lender how likely you are to pay back loan or credit card dues based on your past repayment behaviour. The higher your score, more the chance of your loan application getting approved! If you know your credit score, you can always work towards improving it over a period of time.

## Report any errors in your credit report:

Even if you repay your debt timely, does not mean that you will get excellent credit score. Some errors like inaccurate late payment may pull your score down. And if you are a victim of Identity Theft or credit card fraud, it may show up in your credit report as an extra loan in your name and may even lead to a drop in your credit score. Reviewing your credit report frequently (at least once a year) may help you to check all your credit related information and take necessary measures to correct those inaccuracies (if any).

## Don’t over-apply for new loans or credit cards:

Any new inquiries for loans or credit cards always reflect in your credit report. And too many inquiries may affect your credit score. It is taken negatively by the lenders as the borrower might appear as “Credit Hungry” and also indicates that the debt burden is likely to, or has increased and he/ she is less capable of honouring any additional debt. So, if you have made many applications for loans, or have recently been sanctioned a loan, a Loan provider is likely to view your application with caution.

## Think before closing an old credit card:

Suppose you have a credit card which is 6-7 years old and you are not using that card today. But you have a good credit history on that card. Now if you close this card, then the card issuer will stop sending your payment history or details to the credit bureau. This may lead to drop in your credit score slightly. While over-used cards affect your credit score negatively, the un-used cards, on the other hand strengthen your credit history. It signifies that you have a specific sanction limit but you are not using it as you are financially secure and are not hungry for credit. So, if you can manage, it is advisable to retain your old credit cards even if you don’t use them anymore.

## Credit Card Debt Management

Credit card is a special kind of debt as it is a revolving credit facility along with being the costliest debt in one’s debt portfolio. The interest rates being charged are exorbitant and there is an option to make only a part payment**. These factors make credit card a reason for most of the debt related stress.**

Since you can make part payment, this will impact your future repayment capacity, as more debt gets accumulated, more difficult it will be for you to repay it. Add to that the impact of high rate of interest and this will result in ballooning of interest and what we can call a debt snowball.

Looking at above description credit card may sound as an evil instrument, but if used withing time and within limit credit card can be quite a useful instrument, if you remember the wisdom nugget below.

*“* ***CREDIT CARD IS A CREDIT INSTRUMENT, IT EXTENDS YOU A FREE CREDIT PERIOD OF UPTO 45 DAYS, IT IS NOT TO BE UTILISED AS A DEBT FACIILTY***”

Credit card has been the cause of most debt related stress in the individual, credit card should not be seen as a debt instrument, it should be seen as an instrument of credit extension

* Credit Card debt is the most special kind of debt as it requires most of attention because of the following reasons
* Easily available Credit
* Free Credit Period of 45 days
* Option to make part payment
* Extremely high interest rate
* Ballooning Impact of the interest
* Source of Instant Credit
* Cause of Debt Related Stress in most of the cases

One of the most important things that one should remember about credit card is that there is a facility of making a part payment or you can choose to pay only a minimum amount, this is cause of all the stress.

If you keep on making the part payment in the credit card, it takes in excess of 10 years to repay the debt

***“If you do not pay off the full outstanding amount on the credit card, then the complete outstanding including the new purchases of the next cycle is charged to the interest***.”

Paying off the complete credit card balance within the due date is the key to managing credit card debt.

## Chapter 6- Debt Restructuring

Debt restructuring is a process used by companies, individuals, and even countries to avoid the risk of [defaulting](https://www.investopedia.com/terms/d/default2.asp) on their existing debts, such as by negotiating lower interest rates. Debt restructuring provides a less expensive alternative to [bankruptcy](https://www.investopedia.com/terms/b/bankruptcy.asp) when a debtor is in financial turmoil, and it can work to the benefit of both borrower and lender.

Debt restructuring can be a win-win for both sides because the business avoids bankruptcy and the lenders typically receive more than they would have through a bankruptcy proceeding.

Individuals facing insolvency can try to renegotiate terms with their creditors and the tax authorities. For example, someone who is unable to keep making payments on a INR250,000 0mortgage might reach an agreement with the lending institution to reduce the mortgage to 75%, or INR187,5000 (75% x INR250,0000 = INR187,5000). In return, the lender might receive 40% of the house sale proceeds when it is sold by the mortgagor.

* Debt Restructuring is an integral part of debt advisory/ credit counselling
* The term is more associated with corporate finance, the way the companies manage their debt
* Debt restructuring is a process that is followed by companies, individuals and even countries to avoid the risk of defaulting on their existing debts
* Based on the specific situation, various measures can be advised to the individuals caught in a stressful situation
* Debt restructuring provides a less expensive alternative to bankruptcy when a debtor is in financial turmoil, and it can work to the benefit of both borrower and lender.

**Refinancing of Home Mortgage- A novel way to restructure your debt**

A novel way of debt restructuring is refinancing your home mortgage. Of course, that eliminates some people because they either don’t have their own home yet or, if they do, they don’t have enough equity in that home to make restructuring feasible. But if you do have your own home and you have enough equity, here’s how to use that equity to restructure your consumer debt:

### Qualify Yourself

The first step is to determine how much [equity](https://en.wikipedia.org/wiki/Home_equity) you have in your home. To do that, simply subtract the current balance of your mortgage from the current market value of the home. If your home equity is equal to or greater than the total amount of credit card you have, you might be a good candidate for debt restructuring.

### How It Works

If you determine that debt restructuring is right for you, the next step is to do a [cash out refinance](http://www.zillow.com/mortgage-learning/cash-out-refinance/), and use the cash you receive to pay off your credit card and other high interest debt.

### Why It Makes Sense

Some people will tell you that using cash out refinancing to pay off consumer debt is just trading one debt for another. That’s true. But there are some very real benefits to restructuring in this way:

* Your mortgage interest is much lower than your credit card interest, so you’re saving money there – a lot of it.
* Your mortgage payment is much lower than the total of your current mortgage payment and your consumer debt payments, so you’re saving money there too – potentially a lot, depending on the loan terms and other variables that are unique to your situation.
* You can use the increased discretionary contribute to your savings and retirement plans every month.
* If your cash out is greater than the amount you need to pay off your consumer debt, you can put that extra cash into a separate savings account designated as your emergency reserve. Having an emergency reserve will keep you from having to use plastic when an unforeseen expense arises.

### A Huge Caveat

Of course, as is the case with most good things, there is a caveat to using your cash out refinancing to restructure personal debt. It requires ongoing fiscal discipline to be successful. That means avoiding the credit card trap in the future. If you pay off your credit cards in this way, then run up those balances again, you’ll find yourself in worse financial shape than before. So it’s best to just cut those credit card up (don’t close out the account since it could negatively affect your credit), or at least hide the cards in the freezer or somewhere so that you’re not tempted to use it every time you open your wallet of handbag.

## How does the debt restructure process work?

If you’re seeking debt restructuring with a creditor,

1. **Contact the lender and explain your financial difficulties:**Debt restructuring is a creditor’s response to borrowers who are struggling to afford their bills. Ideally, you’d contact your lender once you realize you won’t be able to afford payments. Reaching out to your lender could be better for your credit than waiting for the lender to contact you, as they’d only do so after you’ve missed payments and already accrued fees.
2. **Wait for a lender response:** Lenders generally aren’t obligated to help you and may stick with the original terms of the loan. If they choose to do so and you can’t pay the bill, you may be charged late fees and your late payments could be reported to the credit bureaus. After falling far behind, your account may be sent to collections — or you could be sued for the debt
3. **If the lender offers help, weigh your options:**The lender may choose to offer temporary hardship assistance or loan restructuring. If there’s a debt restructuring proposal, it could take several forms or there may be different options to choose from, such as an adjusted interest rate or repayment term.
4. **Negotiate with the lender:**You may be able to negotiate the terms of your new contract before accepting a debt restructuring offer. For example, you might try to negotiate a lower payment amount or get fees and accrued interest waived.
5. **Accept the new terms:** If you agree with the new terms for your loan, you’ll need to formally accept and sign the agreement. You’ll then be obliged to follow through with the new agreement and continue paying down your debt.

## What is some debt restructuring alternatives?

* [**Debt consolidation**](https://www.lendingtree.com/debt-consolidation/)**:** With debt consolidation, you’ll take out a new loan or line of credit to pay off your current debts. In doing so, you’re replacing your old debt with a new debt, ideally with different terms like a lower interest rate. A longer repayment period would also lower your monthly payments in exchange for higher overall interest charges.
* **Debt management plan:**Rather than trying to negotiate a debt restructuring agreement with your lender directly, you could work with a non-profit credit counselling organization. The counsellor can negotiate with your creditors on your behalf, and may be able to arrange a debt management plan. Generally, these are available for unsecured debts such as credit cards, and the counsellor may be able to negotiate lower interest rates, lower payments, waived fees and bring your past-due accounts current.
* **Payment forbearance or deferment:**Loan forbearance or deferment allows you to temporarily skip several payments without paying late fees or having your account be reported late to the credit bureaus. These could be good options if you experience a temporary setback, but don’t need or want to permanently change your loan.

## Chapter 7- Tax Benefits on Debt

## Home Loan

## Section 80 C

## Under section 80C of Income Tax Act 1961, if you have taken a home loan, then principal repayment can be deducted from the taxable income up to an upper limit of 150000 in a financial year. This limit of 150000 has to be utilized with all other options like Insurance, Fixed Deposit, ELSS etc.

## What this means is that there is no separate provision for principal repayment on housing loan.

## Section 24 B:

## Under this section, the interest repayment on the housing loan is eligible for deduction from taxable income, up to a limit of 200000 in a financial year. This limit is same if the house is self-occupied or it’s a let-out property

## Joint Property

## If the house is a joint property in the name of husband and wife, then both can claim deductions up to the specified limits, provided they both are paying parts of EMI

## Education loan

## Section 80 E

## Under section 80 E, the Assessee can claim a deduction from the taxable income on account of interest paid on education loan, there is no upper limit on this amount, whatever interest you pay in a particular year can be claimed as a deduction, However, this deduction can be claimed for a maximum of 8 years.

## Point to Note:-

## The principal repayment of the education loan is not eligible for any deductions