

# How to Cut Your Interest Rates



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## Overview

If you have accumulated a lot of debt or are paying high interest to existing creditors, you may be looking at ways that you can reduce the overall interest you are paying. Debt consolidation may be an avenue that you are considering – but there are many different types of companies that advertise debt consolidations and debt consolidation loans. It is important to understand the different types of debt consolidation options advertised as each one carries different risks and benefits and each impacts your credit in different ways.

In this e-book we will discuss the 5 most common types of financial solutions that are often promoted as debt consolidations:

- Unsecured Debt Consolidation Loans
- Mortgages
- Consumer Proposals
- Credit Counselling
- Bankruptcy

After reading this e-book you should be able to differentiate between the different items and make more informed decisions with regard to your finances.

# Chapter 1

## Unsecured Debt Consolidation Loans



## **What is an unsecured debt consolidation loan?**

An unsecured debt consolidation loan is most typically offered by financial companies, credit unions and banks. If approved you will typically be extended the credit through a line of credit or loan. A loan is always better because you will have a pre-fixed term and you will know that at the end, the debt will be paid off. Lines of credit are attractive because they often bear a lower payment than loans – but because they end up taking far longer to pay off at the minimum payments you often end up paying more interest. When the company issues the debt consolidation loan they may pay off your creditors directly or they may just advance the funds to you to pay your creditors. After you have paid off your creditors you should be left with a single monthly payment to your debt consolidation.

## **Who is the best candidate?**

Generally you have to have good credit and be gainfully employed to qualify for an unsecured debt consolidation loan. If you have bad credit or difficulty proving your income you may only qualify with a high interest lender and in this case this product may not make sense.

## **Considerations:**

Check your interest rates! If the interest rate on the debt consolidation loan is higher than the current interest rate you are paying to your cards, think before you commit to this. The lender may pitch you on the reduced, single monthly payment and term but you will end up paying more in the end in many cases.

## **Risks:**

- Could result in more interest being paid
- If you use your credit cards again after consolidating the debt, you could end up in serious financial trouble

## **Benefits:**

- Single monthly payment
- Potentially reduced monthly payment
- Potentially reduced interest rate
- Will clear revolving balances on credit report leading to a higher credit score

**Impact to your credit:**

The impacts of an unsecured debt consolidation loan are positive because revolving balances will be cleared.

# Chapter 2

## Mortgage Refinancing



## **Mortgage Refinancing**

Mortgage refinancing is a viable option that many Canadians use to cut their interest and consolidate debt. More so than debt consolidation, there are many, many different mortgage products and the one that is suitable to you will depend on your credit, the equity positioning in your home and your income type.

This chapter will deal with consolidating debt through:

- Refinancing your first mortgage/arranging a new first mortgage
- Refinancing your second mortgage/arranging a new second mortgage
- Obtaining an equity only second mortgage

## ***First Mortgages***

### **What is a first mortgage?**

First mortgages are arranged when there is no mortgage owing against a home or in the event that there is and you want to refinance it to unlock equity to pay off your debt.

### **Who is the best candidate?**

Generally, someone with less than 80% of the value of the home owing as a mortgage and someone with good credit is the best candidate for this option.

### **Considerations:**

- If you cannot prove your income – you will need more equity (see equity only mortgages).
- If you have problems with your credit – you will need more equity (see equity only mortgages).
- You should confirm that your existing first mortgage is not closed. If it is closed you may not be able to refinance it with a lender other than your existing first mortgage lender or they may allow you to pay it off but charge you big pre-payment penalties.
- Make sure to consider all the costs to do this and how they factor into your overall cost of borrowing: mortgage fees, lender fees, legal fees, appraisal/CMHC fees, penalties for opening your mortgage, etc... These can really add up quickly

so it is important to ask your mortgage agent/broker for a firm estimate at the point when you are applying for a mortgage.

### **Risks:**

- When looking at your new first mortgage term make sure to reduce your amortization according to the amount of new debt you are adding to the mortgage. Discuss this with your mortgage broker. Many who don't address this end up re-extending their mortgage amortization out over the max. number of months. In the end, while you may not see much of an increase to your mortgage payment after adding the new debt, you will end up paying more in the long run.
- Once credit balances are cleared through your consolidation you must be careful not to start using those credit cards again or you could create a serious financial problem.

### **Benefits:**

- Potential reduced monthly payment
- Potential reduced interest rates
- Positive impacts to credit
- A single monthly payment

### **Impact to your credit:**

Refinancing your home to consolidate debt will often have positive impacts to credit, especially when it involves clearing outstanding balances on credit card products. If the mortgage involves paying off your debts, they will be cleared off your credit and often second mortgages aren't reported to the credit report at all.

## ***Second Mortgages***

### **What is a second mortgage?**

You can only obtain a second mortgage when you have an existing first mortgage on your property. A second mortgage sits behind your first mortgage and is completely separate. Second mortgages are usually extended as lines of credit or as a mortgage with a mortgage term and amortization. Interest rates can be very low and vary depending on your credit.

## **Who is the best candidate?**

Those with closed first mortgages, those who want to arrange a more aggressive repayment amortization on their balance, and those who don't qualify for first mortgage refinancing are the best candidates for a second mortgage.

### **Considerations:**

- If you cannot prove your income – you will need more equity (see equity only mortgages).
- If you have problems with your credit – you will need more equity (see equity only mortgages).
- Fixed repayment products are usually better than line of credit products when consolidating debt.
- Just because your first mortgage is amortized over 20-30 years doesn't mean your second mortgage has to be – you can negotiate a 5 year amortization on your second mortgage for example, pay a little bit more monthly and be out of debt sooner.

### **Risks:**

- If you extend the amortization over a long period of time – you will end up paying more interest.
- Beware of 1 year terms. This could result in new administration, lender and legal fees every year which will often be applied to your balance.
- Pay attention to how your interest is accrued: semi-annually vs. monthly vs. daily vs. interest only. This can make a huge difference in the amount of interest you pay in the long run.

### **Benefits:**

- Does not impact your first mortgage
- You have more control over your amortization
- It can be easier to pay off faster because it is separate
- Can be refinanced into your first mortgage on renewal
- Consolidates debt into a single monthly payment

### **Impact to your credit:**

Second mortgages often have a positive impact to credit. If the second mortgage involves paying off your debts, they will be cleared off your credit and often second mortgages aren't reported to the credit report at all.

## ***Equity Only Mortgages***

### **What is an equity only mortgage?**

Equity only mortgages are approved based on the equity you have available in your home, assessed based on a calculation – loan to value (LTV). The loan to value is the % owed against your home divided into the value of your home. Even if you have bad credit or other issues that have caused the bank to decline your mortgage application – you still may qualify for an equity only mortgage.

\*Equity only mortgages often bear the highest interest rates.

### **Who is the best candidate?**

Individuals who have had past problems with credit, individuals who are self-employed and/or can't prove their income, and individuals who have more than 35% equity in their home are the best candidates for an equity only mortgage.

### **Considerations:**

- Typically trust companies, finance companies, credit unions, mortgage investment corporations, mortgage brokers and private individuals extend equity only mortgage financing. An institutional lender is always most advantageous.
- Check the small print and fees. Many private lenders have exorbitant fees built into the fine print. For example, if you don't make a payment you could be subject to default fees, etc...
- Pay attention to your mortgage term and try to avoid 1 year terms where possible. If the term must be 1 year, ask what the fees will be on renewal and to have the amounts written into the mortgage agreement.

### **Risks:**

- Fees can be very high – there will potentially be a broker fee, lender fee, administration fee, legal fee, etc... If you are only looking for \$20k for example, and the fees are up to \$4,000, this product may not make sense.
- Interest only mortgages – private mortgages are often interest only. This means your minimum payment is only based on interest. If you want to reduce your principal – you will have to make more than your minimum payment!

**Benefits:**

- Consolidates debt to a single payment
- Is an option for those who can't get the financing elsewhere

**Impact to your credit:**

Equity only mortgages often have a positive impact to credit. If the equity mortgage involves paying off your debts, they will be cleared off your credit and often second mortgages aren't reported to the credit report at all.

# Chapter 3

## Consumer Proposals



## **What is a Consumer Proposal?**

Many companies promote consumer proposals as a form of debt consolidation and while they do involve a single monthly payment that is often less than the monthly payments being made currently to creditors, it is not actually a debt consolidation loan.

A consumer proposal is an arrangement that's negotiated with your creditors through a bankruptcy trustee. If accepted the applicant ends up making a single monthly payment to the trustee in bankruptcy over a term of usually 4-5 years. The trustee in bankruptcy administers the consumer proposal and represents both the applicant and the creditors. For this reason many applicants will hire their own financial advisor to organize their financial information prior to approaching the trustee in bankruptcy.

Individuals and businesses can make consumer proposals.

You can file a consumer proposal if you have not less than \$5,000 in unsecured debt and not more than \$250,000 in unsecured debt.

The typical process:

- You may or may not choose to seek financial advice prior to approaching the trustee.
- You approach the trustee and the proposal is formulated based on your cash flow and equity.
- The trustee makes the proposal to your creditors.
- Your creditors have approximately 1 month to accept or reject your proposal. If they don't respond they are considered as having accepted the proposal.
- If the majority of your creditors accept your proposal it is legally binding and while you have a minimum monthly payment obligation, you can pay the consumer proposal in full at any time.

## **Who is the best candidate?**

Individuals or business who owe more than \$5,000 and less than \$250,000 in unsecured debt and are struggling to make minimum payments, and/or those with past bad credit reporting on his/her credit report relating to unsecured debts of more than \$5,000.00 and less than \$250,000.

## **Considerations:**

- If you have equity in your assets, a consumer proposal may not be the best option for you.
- If one of your creditors has placed a lien on your home for example, that makes them a secured creditor and this can impact your proposal if the bulk of your debt is owed to them.

**Risks:**

- If your creditors reject your proposal you will have to negotiate something that they will accept.
- There are implications to your credit.

**Benefits:**

- Involves a single monthly payment
- Ensures that debt is paid off within 5 years
- Can be paid in full at any time
- Often reduces the amount of debt
- Often reduces the monthly payment
- Freezes interest
- Stops most collection action – wage garnishments, etc...

**Impact to your credit:**

A consumer proposal will report to your credit report for 3 years from the date it is paid in full. For example: if you pay off the consumer proposal in monthly payments over 4 years, the consumer proposal will remain on your credit for 7 years. If you pay off your consumer proposal in 1 year, then the consumer proposal will only remain on your credit report for 4 years. As soon as you file your proposal it pays to begin rebuilding your credit by securing a secured credit card. Speak with your DebtCare representative and we can send you an application for a secured MasterCard.

# Chapter 4

## Credit Counselling



## **What is a Credit Counselling?**

Legitimate credit counselling agencies are not for profit agencies that arrange programs for individuals who get overwhelmed with debt. Credit counselling agencies are not for profit but do receive funding from banks and other financial institutions. Banks and financial institutions like credit counselling because while a credit counselling program will involve freezing interest it almost never reduces the principal debt so creditors yield a higher repayment than they would have had the individual filed a consumer proposal.

Credit counselling agencies get paid from a portion of the monthly payment that you make into the program.

Credit counselling programs are usually negotiated based on you repaying your debt over a standard term of 5 years at no interest. If approved, you would make a single monthly payment to the credit counselling agency which they then distribute to your creditors.

## **Who is the best candidate?**

Individuals or business who owe less than \$250,000 in unsecured debt and are struggling to make minimum payments, those who don't owe enough money to apply for a consumer proposal, and/or those who want to repay the entire principal debt owing are the best candidates for credit counselling.

## **Considerations:**

- If you have equity in your assets, a credit counselling proposal may not be the best option for you.
- If one of your creditors has placed a lien on your home, for example, that makes them a secured creditor and may result in a credit counselling proposal not being the right option.

## **Risks:**

- If your creditors reject your credit counselling proposal you will have to quickly have a back-up plan
- There are implications to your credit
- These will almost always involve you repaying the full principal balances owing to your creditors

**Benefits:**

- Involves a single monthly payment
- Ensures that debt is paid off within 5 years
- Can be paid in full at any time
- Often reduces the monthly payment
- Freezes interest
- Stops most collection action – wage garnishments, etc...

**Impact to your credit:**

A credit counselling proposal will change the ratings on your trade lines (credit products) to 7s.

They will remain 7s for 3 years from the date the proposal is paid in full. For example: If you pay off the proposal in monthly payments over 4 years, the 7s will remain on your credit for 7 years. If you pay off your proposal in 1 year, then the 7s will only remain on your credit report for 4 years. As soon as you file your proposal it pays to begin rebuilding your credit by securing a secured credit card. Speak with your DebtCare representative and we can send you an application for a secured MasterCard.

# Chapter 5

## Bankruptcy



## What is Bankruptcy?

A bankruptcy is administered by a trustee in bankruptcy and involves a legal process designed to relieve honest but unfortunate individuals of their debts.

At the end of the process, the individual is released from the obligation to repay the debts they had when the bankruptcy was filed (with some exceptions).

Bankruptcies are administered by trustees in bankruptcy. The bankruptcy trustee is impartial and represents both the interests of the bankrupt and that individual's creditors. For this reason, many individuals will consult a financial professional that specializes in insolvency to structure their financial information prior to approaching the trustee in bankruptcy.

## Who is the best candidate?

To go into bankruptcy in Canada, a person must:

- Live or do business in Canada, and must be **insolvent**.
- To be insolvent means:
  - a. To owe at least \$1,000.
  - b. Not to be able to meet your debts as they are due to be paid.

## Considerations:

- Assets with equity – if you have assets like a home and have equity – bankruptcy may not be the right option for you and we highly recommend speaking with a financial advisor before approaching a trustee.
- Surplus income – there is a basic calculation in the BIA that involves subtracting specific expenses from your income and the income left over is deemed “surplus income”. First time bankruptcy filers will have to pay the trustee over a term that depends on whether or not there is surplus income.
  - If there is no surplus income you have to pay into your bankruptcy for 9 months.
  - If there is surplus income you have to pay into your bankruptcy for 21months.

Surplus income can also occur during a bankruptcy in the event that you accumulate equity in assets, or your income increases.

**Risks:**

- You will have ongoing reporting obligations to the trustee. If your situation improves you will often have to pay more into your bankruptcy.
- You cannot pay a bankruptcy in full
- There are implications to your credit

**Benefits:**

- Will almost always significantly reduce the amount of debt that you owe
- Ensures that debt is paid off within 21 months
- Often reduces the monthly payment
- Freezes interest
- Stops most collection action – wage garnishments, etc...

**Impact to your credit:**

A bankruptcy will appear on your credit report for 7 years from when it is filed.

As soon as you file your bankruptcy it pays to begin rebuilding your credit by securing a secured credit card. Speak with your DebtCare representative and we can send you an application for a secured MasterCard.

# Chapter 6

## Comparison Chart

Use this comparison chart to weigh the positives and negatives according to each option.

Benefit	Unsecured Loan	Mortgage	Consumer Proposal	Credit Counselling	Bankruptcy
Pays off debts 100% without freezing interest	X	X			
Can involve paying off debts 100% but freezes interest			X	X	
Can reduce overall debt			X		X
Can reduce monthly payments	X	X	X	X	X
Offers single monthly payments	X	X	X	X	X
Stops collection action like wage garnishments			X	X	X
Involves interest	X	X			
Interest free			X	X	X
Impacts credit positively	X	X			
Impacts credit negatively			X	X	X

## Conclusion

We hope that this e-book has helped you to understand the different debt consolidation options available and which ones can cut your interest. What is most important when looking for ways to cut your interest is to be informed by doing lots of research about the various credit products and consolidation options available. We can see you've already gotten started!

Still feeling lost?

Feel free to set up a free financial consultation and review of your finances with an experienced DebtCare representative.

Here's how to reach us:

- Phone: 1-888-898-0888
- Email: [president@debtcare.ca](mailto:president@debtcare.ca)
- Web: [www.debtcare.ca](http://www.debtcare.ca)

## Author Bio



This e-book was written by Michael Goldenberg. Michael Goldenberg is the founder and President of DebtCare Canada Inc.

DebtCare Canada offers a service for those who struggle with debt. When Michael formed DebtCare Canada he refused to offer the typical ‘credit counselling/debt services’ offered by other credit counselling agencies.

Seeing that many bankruptcy trustees and credit counselling agencies are one dimensional, Michael formed a multi-faceted team.

A group of senior financial consultants, credit counsellors, advocates, accountants and in-house legal counsel offer clients a turnkey solution.

Currently, Michael’s role as President of the organization has him establishing and negotiating strategic partnerships that enable DebtCare Canada to set a new standard in the financial consulting industry. Contact Michael at: [mgoldenberg@debtcare.ca](mailto:mgoldenberg@debtcare.ca).

This e-book will discuss mortgages vs. unsecured debt consolidation vs. consumer proposals vs. credit counselling vs. bankruptcy

There will be one chapter on each – I will help you with points on this when you get to it