

## Get Organized

Create a student loan checklist that lists all of your student loans. A blank form is available at

[www.finaid.org/studentloanchecklist](http://www.finaid.org/studentloanchecklist)

Put all your paperwork for each loan in its own file folder labeled with the lender name, date borrowed, original loan balance and loan id.

Put a note in your calendar at least a week before your first payment is due.

## Don't Miss Payments

One quarter to one third of borrowers are late or delinquent on the very first payment on their student loans. Most student loans have a six-month grace period before repayment begins. Students often move after graduation, losing track of bills. The loan payment is due even if you do not receive a statement or coupon book. Be sure to notify the lender about any changes in address or contact information.

Borrowers who consolidate their federal student loans are more likely to pay on time, with less than one fifth missing the first payment, in part because the first payment is due soon after consolidation.

## Set Up Automatic Monthly Payments

Set up an automatic direct debit from your checking account to make the monthly payments on your loans. Borrowers with auto-debit are much less likely to miss a payment.

Many lenders offer discounts for borrowers who set up auto-debit. Federal loans offer a 0.25% interest rate reduction while private student loans often offer a 0.25% or 0.50% interest rate reduction for the remainder of the repayment period. Some lenders will require electronic billing to get the discount.

## Accelerate Repayment of High Interest Debt First

Student loans do not have prepayment penalties. Making an extra payment can save you money. After you make the requirement payments, direct any extra money toward accelerating repayment of the most expensive debt first. The most expensive debt is the debt with the highest interest rate, not the lowest monthly payment. Usually this is credit card debt and private student loans. Paying an extra \$100 on a 10% loan is like earning 10% interest, tax-free, and may save you more than \$200 over the life of the loan depending on the type of loan.

## Student Loan Interest Deduction

You may be able to get a few hundred dollars back on your federal income taxes for the interest you pay on your federal and private student loans. Up to \$2,500 in student loan interest may be deducted each year. The deduction is an above-the-line exclusion from income and can be taken even if you don't itemize. The deduction is not affected by the higher "alternative minimum tax" (AMT) like the mortgage interest deduction. Only the borrower responsible for making payments can take the deduction. You must also not be claimed as an exemption on someone else's tax return.

### Key Student Loan Resources

#### FinAid's Student Loans Section

[www.finaid.org/loans](http://www.finaid.org/loans)

#### FinAid's Student Loan Calculators

[www.finaid.org/loans/calculators.phtml](http://www.finaid.org/loans/calculators.phtml)

**Forgot Your Lender?** Ask your college's financial aid administrator or visit [www.finaid.org/lostlender](http://www.finaid.org/lostlender)

#### Student Loan Borrower Assistance Project

[www.studentloanborrowerassistance.org](http://www.studentloanborrowerassistance.org)

#### Federal Student Loan Consolidation

[loanconsolidation.ed.gov](http://loanconsolidation.ed.gov)

1-800-557-7392 or TTY 1-800-557-7395

#### Private Student Loan Consolidation

[www.finaid.org/privateconsolidation](http://www.finaid.org/privateconsolidation)

#### US Department of Education's Debt Collection Service and Default Resolution Group

[www.ed.gov/offices/OSFAP/DCS/](http://www.ed.gov/offices/OSFAP/DCS/)

1-800-621-3115 or TTY 1-877-825-9923

[drghelp@ed.gov](mailto:drghelp@ed.gov)

#### Federal Student Aid Ombudsman

The FSA Ombudsman mediates disputes and helps resolve problems concerning federal student loans.

[www.ombudsman.ed.gov](http://www.ombudsman.ed.gov)

1-877-557-2575 or fax 1-202-275-0549

[fsaombudsmanoffice@ed.gov](mailto:fsaombudsmanoffice@ed.gov)

#### Federal Student Aid Information Center

1-800-4-FED-AID (1-800-433-3243) or 1-319-337-5665

1-800-730-8913 TTY

## Tradeoffs of Federal Student Loan Consolidation

Federal student loan consolidation streamlines repayment by replacing several loans with a single loan. The interest rate on a federal consolidation loan is the weighted average of the interest rates on the original loans, rounded up to nearest 1/8<sup>th</sup> of a point and capped at 8.25%. The use of the weighted average preserves the costs of the loans, so consolidation usually does not save money.

Consolidation provides access to alternate repayment plans which reduce the monthly payment by increasing the loan term, but this will also increase the total interest paid over the life of the loan. Consolidation can also be used to switch lenders. But borrowers who consolidate lose the remainder of the grace period on their loans. They also lose favorable benefits on Federal Perkins loans such as subsidized interest and loan forgiveness.

It may not be necessary to consolidate to simplify repayment or get a lower monthly payment. Many lenders offer unified billing which provides a single bill for all your student loans. Some alternate repayment plans are available without consolidation, such as extended repayment and income-based repayment.

## Tradeoffs of Private Student Loan Consolidation

Like federal consolidation, private student loan consolidation replaces several private student loans with a single loan. The new loan has a variable interest rate just like the original loans, but the new rate is based on your current FICO (credit) scores. So if your credit score has improved significantly (say, because you've graduated, got a good job and have been paying all your bills on time), you might be able to get a better interest rate. Private consolidation may also be used to remove the cosigner from a loan if the new consolidation loan does not include a cosigner. (Some lenders offer a cosigner release option which removes the cosigner from the loan without consolidation if the primary borrower has excellent credit and has made the first 24, 36 or 48 payments on time.) Note that federal and private student loans cannot be consolidated together.

Repayment Plan	Monthly Loan Payment	Total Interest	Total Loan Payments
Standard – 10 Years	\$288	\$9,524	\$34,524
Extended – 12 Years	\$254	\$11,639	\$36,639
Extended – 15 Years	\$222	\$14,946	\$39,946
Extended – 20 Years	\$191	\$20,802	\$45,802
Extended – 25 Years	\$174	\$27,054	\$52,054
Extended – 30 Years	\$163	\$33,674	\$58,674

Assumes \$25,000 unsubsidized Stafford loan at 6.8% interest and ignores balance-based setting of extended repayment term.

## Federal Student Loan Repayment Plans

There are four main types of federal student loan repayment plans: Standard Repayment (10-year term), Extended Repayment (10- to 30-year term), Income-Based Repayment (payments based on income) and Graduated Repayment (low payments are increased every two years). Either income-based repayment or extended repayment will yield the lowest monthly payment.

### Extended Repayment

If you have more than \$30,000 in federal student loans with a single lender you can get 25-year repayment without consolidating. Otherwise you can consolidate to get up to a 30-year repayment term based on the loan balance, as illustrated in this table.

Debt	Loan Term
Less than \$7,500	10 years
\$7,500 to \$9,999	12 years
\$10,000 to \$19,999	15 years
\$20,000 to \$39,999	20 years
\$40,000 to \$59,999	25 years
\$60,000 or more	30 years

### Impact of Extended Repayment

The next table shows the impact of extended repayment on the monthly loan payment and the total interest paid on an unsubsidized Federal Stafford loan as compared with standard 10-year repayment.

Extended Repayment Loan Term	Reduction in Size of Monthly Loan Payment	Increase in Total Life-of-Loan Interest
12 years	12%	22% (factor of 1.22)
15 years	23%	57% (factor of 1.57)
20 years	34%	118% (factor of 2.18)
25 years	40%	184% (factor of 2.84)
30 years	43%	254% (factor of 3.54)

Switching from a 10-year term to a 20-year term will cut the monthly payment on an unsubsidized Stafford loan by a third but will also more than double the total interest paid over the life of the loan. This adds thousands of dollars in extra interest to the cost of the loan, more than \$4,500 extra for every \$10,000 borrowed. With a 25-year term you'll pay more in interest than the original amount borrowed.

With a 20-year term on a 10% private student loan you'll pay more in interest than the original amount borrowed. Increasing the term from 20 years to 30 years will cut the monthly payment by less than a tenth but will increase the total interest paid by almost two-thirds.

## Income-Based Repayment (IBR)

Income-based repayment (IBR) bases the monthly payments on a percentage of *discretionary income*, not the amount owed. Discretionary income is defined as the adjusted gross income (AGI) minus 150% of the poverty line for the family size. Currently IBR caps the monthly payments at 15% of discretionary income. If a borrower's AGI is less than 150% of the poverty line, the monthly payment under income-based repayment is zero. The remaining debt and interest will be forgiven after 25 years in repayment. (A new version of IBR will cut the monthly payments by one third to 10% of discretionary income. It will also accelerate the loan forgiveness to 20 years. These changes are not retroactive and are available only to new borrowers of new loans on or after July 1, 2014.)

## Public Service Loan Forgiveness

Public service loan forgiveness accelerates the forgiveness under income-based repayment to 10 years and makes it tax-free. Only federal student loans are eligible. Private student loans are not eligible. You must be employed full-time for 10 years in a public service job, such as police, fire, EMT, government, military, public education, public health, social work, public interest law, public librarian and 501(c)(3) organizations. The loan forgiveness is not retroactive, so prior employment in a public service job does not count. If the loans are not already in the Direct Loan program, they can be moved into the Direct Loan program by consolidating them (even if the loans were previously consolidated). Public service loan forgiveness will generally yield a financial benefit if the borrower's federal student loan debt exceeds his or her income.

## Dealing with Financial Difficulty

There are more options for dealing with financial difficulty on federal student loans than on private student loans. A temporary suspension of loan payments is best for short-term financial difficulty, such as maternity or medical leave, or short-term unemployment. Examples of temporary suspensions include the economic hardship deferment (3 year limit) and forbearances (5 year limit). Changing repayment plans is a better option for longer-term financial difficulty, such as a high debt to income ratio. Examples include income-based repayment and extended repayment, both of which reduce the monthly loan payment. (If your circumstances improve, you can change the repayment plan back to a shorter term. You can change repayment plans once a year.) All of these options will ultimately increase the cost of the loan by increasing the total interest paid over the life of the loan. But they are better than defaulting on the loan, which also adds fees and penalties.

## Temporary Suspensions of Payments

Monthly payments of principal and interest are suspended during a deferment or forbearance. The difference between a deferment and a forbearance is who pays the interest. The government pays the interest on subsidized loans during deferments only. The borrower is responsible for the interest on unsubsidized loans during a deferment and on all loans during a forbearance. The borrower may defer interest by capitalizing it, which increases the amount owed. Extended periods of non-payment can cause the loan balance to get much larger. It is better to pay at least the interest if you can afford it. Before using a deferment or forbearance, consider whether income-based repayment may be more suitable.

## Debt Grows with Capitalized Interest

Capitalized interest is a form of negative amortization, digging you into a deeper hole because the interest continues to accrue and is added to the loan balance. You will also end up paying interest on interest. Extended periods of nonpayment will cause your loan to grow much bigger, as is illustrated by this chart.

Forbearance Duration	Capitalized Interest	Increase in Loan Balance	Increase in Life-of-Loan Interest
<b>3 months</b>	\$171	1.7%	\$236 (6.2%)
<b>6 months</b>	\$345	3.4%	\$476 (12.5%)
<b>1 year</b>	\$702	7.0%	\$967 (25.4%)
<b>3 years</b>	\$2,256	22.6%	\$3,115 (81.8%)
<b>6 years</b>	\$5,021	50.2%	\$6,933 (182.0%)
<b>9 years</b>	\$8,409	84.1%	\$11,613 (304.8%)
<b>12 years</b>	\$12,562	125.6%	\$17,348 (455.4%)
Increases in loan costs from capitalized interest on a \$10,000 Stafford loan with a 6.8% interest rate and a 10-year loan term			

## Get Written Confirmation of Changes

Keep notes during any telephone call with a lender, including the date and the name of the person with whom you spoke. Ask for confirmation numbers for any changes. Ask the lender to send you written confirmation and call the lender if you don't receive it within a week. Continue paying the loans until you receive written confirmation of a deferment or forbearance. Send forms by certified mail, return receipt requested.

## Talk to the Lender before You Default

There are many options, such as deferments and forbearances, that may help prevent you from defaulting on your loans. You will lose access to these options if you default on your loans first. Ignoring the problem will not make it go away; it just digs you into a deeper hole as interest continues to accrue.

## Penalties for Defaulting on Your Loans

The penalties for defaulting on your loans can be quite severe. The federal government has strong powers to compel payment. The government can garnish (seize or withhold) up to 15% of your wages and Social Security benefits and intercept (offset) your federal and state income tax refunds and state lottery winnings. You may be charged late fees of up to 6% of each late payment. Collection charges of up to 25% may also be deducted from each payment on your defaulted loans, slowing the repayment trajectory and increasing your costs. The government can block the renewal of professional licenses. The default may prevent you from getting credit cards, auto loans and home mortgages and may make it harder to rent an apartment or get a job. You will be ineligible for more federal student aid. You may be harassed by collection agencies.

## Loan Rehabilitation

Rehabilitation is a one-time opportunity to remove a federal student loan default from your credit history and to regain student aid eligibility. You will be able to consolidate the defaulted federal student loans after making 3 consecutive full and voluntary on-time payments or if you agree to repay the debt using income-based repayment. You will regain eligibility for federal student aid after making 6 consecutive full and voluntary on-time payments. After you've made 9 of 10 consecutive on-time payments, you can apply to have the loan rehabilitated and the default removed from your credit history. Voluntary payments do not include wage garnishment or offset of income tax refunds. On-time is defined as within 15 days of the due date for regaining student aid eligibility and consolidation and within 20 days for rehabilitation.

## Loan Cancellation

Federal student loans offer several loan cancellation provisions.

**Closed School Discharge.** If the college closed while you were in attendance or up to 90 days after withdrawal.

**Unpaid Refund.** If you withdrew and the college owed you or the lender a refund but never returned the funds to the lender.

**False Certification Discharge.** For improper certification of ability to benefit from college or for victims of identity theft.

**Death Discharge.** If the borrower (or the student for whom a parent borrowed a Parent PLUS loan) dies.

**Total and Permanent Disability Discharge.** If a doctor certifies that the borrower is totally and permanently disabled, or if a veteran is unemployable due to a service-connected condition.

## Bankruptcy Discharge

It is very difficult to get student loans discharged in bankruptcy. Less than 1% of bankrupt borrowers succeed in getting student loans discharged because of the requirement to demonstrate undue hardship in an adversarial proceeding. Undue hardship is a present and future inability to repay the debt and maintain a minimal standard of living even after exhausting options for repayment relief and cutting living costs. Discharge is more likely if the financial difficulty was due to circumstances beyond your control. Discharge is also more likely on private loans than on federal loans, since there are fewer options for repayment relief (e.g., disability discharge) on most private student loans.

## Settling Defaulted Federal Student Loans

If you want to pay off your defaulted federal student loans with a lump sum payment, try negotiating a lower settlement. Ask for a waiver of collection charges and offer either the current principal balance plus half of the accrued but unpaid interest or at least 90% of the current principal and interest balance. Get the compromise offer in writing and have an attorney review it to ensure that it will satisfy all debts in full. Keep the "paid in full" statement in case of future problems.

## Budgeting Tips for High Debt Students

Start with a *descriptive* budget, where you track and categorize all spending for a month. Record the spending each night in a spreadsheet or a program like Quicken or Microsoft Money (or a free version like Mint.com or GNUcash.org). Distinguish mandatory spending (needs) from discretionary spending (wants) and classify your spending into broad expense categories such as food, clothing, shelter, healthcare, transportation, taxes, student loans, entertainment. Also generate subtotals by vendor to identify excessive spending.

If your total mandatory spending exceeds your total income, you have a serious problem that cannot be solved just by controlling discretionary spending. You may need to switch repayment plans or get a second job on weekends.

If your total income exceeds your total mandatory spending, you can get your budget under control by eliminating some discretionary spending. Try substituting lower cost options, such as living with your parents to save on rent, cut luxuries like cable TV and cell phone service, and sell extra belongings.

Avoid credit cards, as spending \$500 on a credit card feels the same as spending \$5, so it is harder to exercise restraint when you pay with plastic.