Confronting Student Loan Debt

Take steps on creating a plan of action to confront student loan debt

At the end of 2012 , Americans owed close to $1 trillion in student loan debt.

The average loan debt is about $25,000.

Forty one percent (41%) of all student loans are delinquent in the first five years of repayment.

Step 1-Identify the types of student loans you owe

Each student loan product has different repayment requirements.

The most common student loan is the **Federal Direct Stafford,** available subsidized and unsubsidized. For both types, repayment is not due until six months after the student leaves school. **Perkins loans** are a type of subsidized student loans with a fixed interest rate that does not start accruing interest until repayment starts, which is typically nine months after the student leaves school.

PLUS (Parent Loans for Undergraduate Students) are federally-backed loans that can be made to parents and graduate students. The interest rate is fixed and has no grace period. Repayment begins immediately after the student leaves school.

If the borrower has **Private Student Loans,** they generally come in two types: school-channel and direct-to-consumer. School-channel loans have the lowest interest rates but generally take longer to process. They are "certified" by the school, which means the school signs off on the borrowing amount and the funds are disbursed directly to the school. Direct-to-consumer private loans are not certified by the school. In fact, schools do not interact with a direct-to-consumer private loan at all. The student simply supplies enrollment verification to the lender, and the loan proceeds are disbursed directly to the student. Both types have high limits that can be borrowed by the students but they also come with a higher interest rate. Typically, no payment is due until after the student leaves school, but the interest begins to accrue immediately.

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Step 2: Locate who is servicing your student loans

A great starting point is to visit the **National Student Loan Data System's Student Access (NSLDS).** This is the U.S. Department of Education's central database for federal student loans and grants. A list will be generated of the federal loans received by the borrower. The servicer of each loan will be listed with contact information. Once the borrower identifies the loan servicer, the borrower can access information about repayment terms and repayment start dates.

If it is a Perkins loan, the loan servicer will most likely be the school the borrower attended when the loan was received. But in some cases, the school will have a separate organization handle the billing and other services for the Perkins Loan.

There is no central location listing all of a borrower's private loans. It is the borrower's responsibility to keep track of where they secured these loans. With private student loans, payments are made to the lender, the organization that made the loan initially. The lender provides the borrower with information about repayment terms and repayment start date.

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Step 3: Understand the terms of your student loan

Often times, borrowers have not taken the time to fully read the **promissory notes/contracts** for their loans. By doing this tedious but extremely important task, the borrower receives a clear understanding of what their obligations are on the loan. It will also clarify what type of student loan they have, whether it is a Federal student loan or private student loan.

When it comes to the terms of your student loan, investigate what the grace period is for each of your loans. The **grace period** is a set period of time a borrower graduates, leaves school or drops below half-time enrollment has before they must begin repaying the loan. The purpose of the grace period is to give the borrower time to get financially settled and to select a repayment option. Not all federal student loans have a grace period, such as a Parent Plus loan. Most loans have a grace period that ranges from six to nine months. If a borrower is called to active military duty for more than 30 days before the end of their grace period, they are eligible to receive the full six months grace period when they return from active duty.

If you fail to make payments on your student loans once the grace period is up, you are in **default** of the loan's contract and there are consequences. Because these loans are backed by the federal government you will always have to pay them back. They are exempted from bankruptcy. The federal government can garnish up to 15% of your wages and social security as well as any federal income tax refund. There will also be collection charges of up to 25% deducted from each payment which in turn increases the amount you will ultimately repay. These defaults will be reported to the credit reporting agencies. Consequently, this can prevent you from getting credit for other major purchases such as a home or car. It will cause ineligibility for more federal financial aid and will prevent renewal of professional licenses.

It is extremely important to be fully informed about your obligation regarding repayment of student loans. Taking the time to understand these obligations can alleviate being in default and causing financial hardship. Read the promissory notes for each loan you have or apply for to be clear about what your responsibilities will be.

Step 4-Know your repayment options

In the last few years, the federal government has increased the options available to assist borrowers to successfully fulfill their obligations. **Standard and graduated repayment plans** have been the typical repayment options. Both repayment plans are for federal loans. On the standard repayment plan, payments are a fixed amount of at least $50 per month. You have up to 10 years to pay back and will pay less interest. On a graduated repayment plan, the payments are lower at first and then increase usually every two years. You also have 10 years to pay the loan back.

New repayment options include: Extended Repayment Plan, Income-Based Repayment Plan (IBR), Pay-as-You-Earn Repayment Plan, Income-Contingent Repayment Plan, and Income-Sensitive Repayment Plan. All of these plans are for federally-backed student loans only. For specific details on each of these repayment plans go to: http://studentaid.ed.gov/.

On the Federal Perkins Loan, the repayment plan options are different the other federal student loans. Check with the school you attended while receiving this loan for more information on Perkins Loan repayment plans.

Step 5-Consolidation, Deferment, Forbearance and Forgiveness of Student Loans

Consolidations of student loans are one of the most popular options for managing repayment of student loans. This option streamlines repayment by replacing multiple loans with a single loan. Student loan borrowers are eligible to consolidate their loans generally after they graduate, leave school or drop below half time enrollment. Consolidation also provides access to other repayment plans that may reduce the monthly payment by stretching out the loan term. This option can also increase the total cost of the loan which generally means the borrower will not save money by selecting this options but simply make the repayment more manageable. It is recommended that student loan borrowers review each of the federal loans they have to make sure they are utilizing the best repayment option before consolidating their student loans. A **PLUS loan** made to a parent of a dependent student cannot be transferred to the student through consolidation. Therefore, a student who is applying for consolidation cannot include the PLUS loan their parents may have taken out for education.

For a complete list of the federal student loans eligible for consolidation, contact the **Direct Loan Consolidation Center** by calling 1-800-557-7392 or visiting www.loanconsolidation.ed.gov.

Private loan consolidation is more complicated. Some private loans can't be consolidated. If the private student loan is already in default, the borrower is required to meet certain requirements before they can consolidate the loan. Typically the new loan, if allowed, has a variable interest rate and is based on the borrower's current credit scores. If the private student loan has a cosigner, often consolidation will remove the cosigner from the loan.

Under certain circumstances, the borrower can receive a **deferment or forbearance** that allows them to temporarily postpone or reduces their federal student loan payments. Postponing or reducing the payments may help the borrower avoid default on the loan. The borrower will need to work with the loan servicer to apply for deferment or forbearance. It is important that the borrower continue to make payments on their loan until the deferment or forbearance is in place.

During deferment the borrower will need to make interest payments on their loan. On the Federal Perkins Loan, Direct Subsidized Loans and Subsidized Federal Stafford Loans, the government may pay the interest. The borrower is responsible for paying interest on all unsubsidized and PLUS loans. If the interest is not paid during deferment, it may capitalize and the account balance will grow. There is a three year limit on economic hardship deferments and a five year limit on forbearances. Temporary suspension of loan payments is a great option for short-term financial difficulties.

Student loans must be paid even if the borrower does not complete their education, can't find a job or is unhappy with the education they received. However, certain circumstances might lead to the student loan being forgiven, cancelled, or discharged. Forgiveness, cancellation and discharge of a student loan means that the borrower is no longer expected to repay the loan.

In 2007, congress created the **Public Service Loan Forgiveness Program** to encourage individuals to enter and continue to work full time in public service jobs. The borrower must make 120 payments on their student loans. If they have fulfilled their obligation working in an approved public service job, their balanced owed will be forgiven. Only Direct Loans are eligible.

Cancellation of student loans is very difficult to receive and only applies to federally funded student loans. The following are events that may make loan cancellation an option:

- Closed School Discharge: If the college closes while the borrower was in attendance or up to 90 days after withdrawal.
- Unpaid refunds: If a borrower withdrew and the college owed a refund but never returned the funds to lender.
- False Certification Discharge: If the college improperly certified the borrower's ability to benefit from a higher education or the borrower is a victim of identity theft.
- Death Discharge: If the borrower (or 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 unemployed due to a service-connected condition they may be eligible for this discharge.

Free financial education is available to assist consumers in understanding the process of building and maintaining their credit.

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