FINANCING A COLLEGE EDUCATION

by Dominic Lucente

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A primer for parents and grandparents.

A university education can often require financing and assuming debt. If your student fills out the Free Application for Federal Student Aid (FAFSA) and does not qualify for a Pell Grant or other kinds of help, and has no scholarship offers, what do you do? You probably search for a student loan.

A federal loan may make much more sense than a private loan. Federal student loans tend to offer kinder repayment terms and lower interest rates than private loans, so for many students, they are a clear first choice. The interest rate on a standard federal direct loan is 4.45%. Subsidized direct loans, which undergraduates who demonstrate financial need can arrange, have no interest so long as the student maintains at least half-time college enrollment.[1,2]

Still, federal loans have borrowing limits, and those limits may seem too low. A freshman receiving financial support from parents may only borrow up to $5,500 via a federal student loan, and an undergrad getting no financial assistance may be lent a maximum of $57,500 before receiving a bachelor's degree. (That ceiling falls to $23,000 for subsidized direct loans.) So, some families take out private loans as supplements to federal loans, even though it is hard to alter payment terms of private loans in a financial pinch.[1,2]

You can use a student loan calculator to gauge what the monthly payments may be. There are dozens of them available online. A standard college loan has a 10-year repayment period, meaning 120 monthly payments. A 10-year, $30,000 federal direct loan with a 4% interest rate presents your student with a monthly payment of $304 and eventual total payments of $36,448 given interest. The same loan, at a 6% interest rate, leaves your student with a $333 monthly payment and total payments of $39,967. (The minimum monthly payment on a standard student loan, if you are wondering, is typically $50.)[3]

When must your student start repaying the loan? Good question. Both federal and private student loans offer borrowers a 6-month grace period before the repayment phase begins. The grace period, however, does not necessarily start at graduation. If a student with a federal loan does not maintain at least half-time enrollment, the grace period for the loan will begin. (Perkins loans have a 9-month grace period; the grace period for Stafford loans resets once the student resumes half-time enrollment.) Grace periods on private loans begin once a student graduates or drops below half-time enrollment, with no reset permitted.[4]

What if your student cannot pay the money back once the grace period ends? If you have a private student loan, you have a problem – and a very tough, and perhaps fruitless, negotiation ahead of you. If you have a federal student loan, you may have a chance to delay or lower those loan repayments.[3]

An unemployed borrower can request deferment of federal student loan payments. A borrower can also request forbearance, a deferral due to financial emergencies or hardships. Interest keeps building up on the loan balance during a forbearance, though.[1]

At the moment, federal student loans can be forgiven through two avenues. The first, the Public Service Loan Forgiveness (PLSF) program, requires at least 10 years of public service, government, or non-profit employment, or at least 120 student loan payments already made from the individual. The second avenue, income-driven repayment plans, first lowers the monthly payment and extends the payment timeline based on what the borrower earns. If the balance is finally forgiven, the loan forgiveness is seen by the Internal Revenue Service as taxable income. (If you have student loan debt forgiven via the PLSF, no taxes have to be paid on the amount.)[1,3]

Consult financial aid officers and high school guidance counselors before you borrow. Get to know them; request their knowledge and insight. They have helped other families through the process, and they are ready to try and help yours.

Lastly, avoid draining the Bank of Mom & Dad. If your student needs to finance a college education, remember that this financial need should come second to your need to save for retirement. Your student has a chance to arrange a college loan; you do not have a chance to arrange a retirement loan.

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Citations:

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2- www2.cuny.edu/financial-aid/student-loans/federal-direct-loans/ [4/19/18]

3 - credible.com/blog/refinance-student-loans/how-much-will-you-actually-pay-for-a-30k-student-loan/ [12/4/17]

4 - discover.com/student-loans/repayment/student-loans-semester-off.html [8/3/17]