Made Plain

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CHAPTER 1
TYPES OF FEDERAL STUDENT LOANS

There are two federal student loan programs: Direct Loans and Perkins Loans. A few years ago, there was another federal student loan program: the Federal Family Educational Loan program. For one reason or another, Congress scrapped that program. Loans remain outstanding from that program (and other minor programs), however. And because they remain outstanding, those loans remain an issue for borrowers.

Here's a brief breakdown of the Direct Loan, Perkins Loan, and FFEL Loan programs.

Direct Loans

Congress created the Direct Loan program as part of the Student Loan Reform Act of 1993. Under this program, the federal government directly issues loans to the student. The Direct Loan program was designed to cut the middlemen — private lenders and guaranty agencies — from the loan origination process.

The decision to cut middlemen from the loan process made so much sense that almost two decades later Congress eliminated Federal Family Education Loans. By doing that, Congress made Direct Loans the main source of federal student loans for borrowers.

◆ Read more about how the government came to be your student lender at: http://www.huffingtonpost.com/2013/07/19/history-of-student-loans_n_3622709.html.

The Direct Loan Program offers three types of federal student loans:

- Stafford loans (which can be subsidized or unsubsidized);
- PLUS Loans (originally named Parent Loans for Undergraduate Students); and
- Consolidation Loans.

Direct Stafford Loans (Subsidized and unsubsidized)

The government offers subsidized Stafford Loans to undergraduate students who've demonstrated financial need. The loan is subsidized because the borrower doesn't pay interest before repayment begins or during any deferment.

Unsubsidized student loans are awarded to any qualifying borrower, regardless of financial need. The loan is unsubsidized because the borrower is responsible for interest charged during all periods — even when the borrower is in school, in a grace period, or in a deferment.

Direct PLUS Loan

A Parent PLUS Loan allows a parent to borrow a loan to help pay for the education of her child attending an undergraduate school. Unlike other federal student loans, the borrower has to be credit worthy to get the loan.

◆ Get tips on what to do if you were denied a Parent PLUS Loan because of your credit at: https://www.edvisors.com/college-loans/terms/adverse-credit-history/.

A Graduate PLUS Loan allows you to borrow enough money in federal student loans to cover the full cost of graduate school, including reasonable living costs, if you're a graduate or professional degree student. Like Parent PLUS Loans, you must be credit worthy to get the loan. If rejected, you may still get the Graduate PLUS Loan. But you'll have to find a credit worthy cosigner.

Credit worthiness for Parent & Graduate PLUS Loans is measured by federal regulations rather than your FICO score. Those regulations say that you must not have an adverse credit history to be eligible for a PLUS Loan. You have an adverse credit history if you're at least 90 days delinquent on any debt or if you have a derogatory event on your report in the past five years. A derogatory event can be a:

- default status;
- bankruptcy discharge;
- foreclosure;
- repossession;
- tax lien;
- wage garnishment; or a
- write-off of a Title IV debt.

Even if you have an adverse credit history and can't get a cosigner, you still may get a PLUS Loan. To get the loan, you'll have to prove to your lender that extenuating circumstances exist.

Direct Consolidation loan

A Direct Consolidation Loan lets you combine your federal student loans into one loan. The benefits of consolidation include:

- Escaping default quickly;
- Having to make just one monthly payment to one servicer;
- Reducing your monthly payment by extending your payment term (borrowers usually enroll in income-based-repayment, which has a 25 year repayment term); and
- Lowering your interest rate (borrowers with older loans benefit the most because those loans typically have higher interest rates or variable interest rates, or both.)

Visit studentloans.gov to apply for consolidation.

◆ Learn more about consolidating your loans at http://www.nerdwallet.com/blog/nerdscholar/2013/consolidate-student-loans/.

Joint Consolidation Loan

Before 1 July 2006, the Department of Education offered one other type of consolidation loan: the joint consolidation loan. This loan was for married borrowers who agreed to combine their federal student loan debt and to each be held responsible for the new loan. And even if they later divorced, they each remained liable for the entire loan. As Kanye told Jay, “That shit cray.”

◆ Joint consolidation loans have special rules when it comes to payment plans, forgiveness, and cancellation. I highlight those difference in the appropriate sections of this book.

Perkins Loan

Unlike Direct Loans, Perkins Loans are originated and serviced by schools — not the government. (Perkins Loans are backed by the federal government.) Because the school is the lender, all payments and requests for a lower payment amount, deferment, forbearance, forgiveness, and cancellation must be made to the school.

Federal Family Education Loan

Congress created the FFEL program as part of the Higher Education Act of 1965. Under the program, private lenders — as opposed to the federal government — loaned money to students. The federal government guaranteed those loans. So if a borrower ever failed to repay his FFEL loan the government would buy the loan to try and collect it.

There used to be four different types of FFEL Loans:

- Subsidized Federal Stafford Loans;
- Unsubsidized Federal Stafford Loans;
- FFEL PLUS loans; and
- FFEL Consolidation Loans.

FFEL loans stopped being issued in 2010. Now all federal student loans are issued under the Direct Loan Program.

◆ Curious about the FFEL program's creation? Read more at: http://www.dailyfinance.com/2010/03/30/how-the-banks-student-loan-gravy-train-finally-got-halted/.

CHAPTER 2
KNOWING WHO YOU OWE

It's crazy how many of my clients had no clue who they owed their student loans. They didn't know if their loans were federal or private or if their loans were with Navient or FedLoan Servicing. They just knew that they owed a lot of money.

Because they didn't know who they owed, before we could develop their repayment strategy we had to get that information. The easiest way to do that is to access the National Student Loan Data System. That System has information on all your federal student loans.

You access the system by using your personal identification number. That PIN is the same one you used to e-sign your FAFSA paperwork. (If you can't remember that PIN, visit pin.ed.gov.)

Once you're in the System, you'll be able to tell:

- When you first borrowed the loan;
- Whose your current servicer;
- Whose your current lender;
- Whose your current guaranty agency; (You'll have a guaranty agency if you have a Federal Family Education Loan;)
- How much you owe in principal and interest;
- What's your interest rate and whether that rate is fixed or variable; and
- The status of your payment. (Are you current, late, or in default? Or are you in deferment or forbearance?)

You might notice that one company, say Great Lakes Higher Education, has more than one role with your student loan. There's nothing inherently wrong with that company handling multiple roles. It just might make it confusing for you to keep track of who is doing what with your loans.

Once you have your federal student loan information, store it all in one place. I store mine on a Google Docs spreadsheet. A few of my clients are more old school than Blue (You're my boy Blue!) and prefer to use pen and paper. Whether you prefer Sheets or pen a paper, choose a tool, use the tool, and track your loans. It makes repayment much easier.

CHAPTER 3
REPAYING YOUR LOANS

Talk all the noise you want about your federal student loans but they're much better than your private student loans. Unlike your favorite Sallie, the government makes it easy — some say, too damn easy — to pay them back for financing your education.

You have four major repayment options to choose from:

- Standard Repayment;
- Pay As You Earn;
- Income-Based-Repayment; and
- Income-Contingent-Repayment.

When your six month grace period ends, you're automatically enrolled in the Standard Repayment plan. If you want to be enrolled in one of the income-driven-repayment plans — that is, the PAYE, IBR, and ICR plans — submit the IDR plan application designating which of the three you want to be enrolled in to each of your student loan servicers. Depending on your servicer, you can submit your IDR application online, by mail, or by fax.

◆ To get an estimate of your monthly payment under each of the plans, use the Department of Education's repayment estimator at: https://studentloans.gov/myDirectLoan/mobile/repayment/repaymentEstimator.action.

Let's break down the four plans so you understand how each works.

Standard Repayment

The Standard Repayment plan, which is available for all your federal student loans, is the cheapest and fastest way to repay your federal student loans. It's the cheapest because you'll pay less in interest compared to the IDR plans. And it's the fastest because you'll finish repaying your loans within 10 years. (The IDR plans all take at least 20 years to complete.)

Those are the benefits of the Standard plan.

There's a major drawback though: your monthly payment will be higher under the Standard plan than it would under any other.

Pay As You Earn

In 2011, President Obama caused the PAYE plan to be launched. The PAYE plan, which lasts for 2o years, promises to help student loan borrowers deal with their debt by capping borrowers' monthly payments at 10% of their discretionary income. And no matter what a borrower's income is, the amount she would pay under the PAYE plan will never be greater than what her payment would be under the Standard Repayment plan.

That capped monthly payment amount is just one of the PAYE plan's benefits. Other benefits include:

- not capitalizing your interest if you have a partial financial hardship and capping your capitalized interest at 10% if you have no partial financial hardship;
- granting you a partial interest subsidy for your first three years of repayment;

- allowing your payments to be eligible for the Public Service Loan Forgiveness program; and
- forgiving any remaining balance after you've made 20 years of payments.

There are at least three drawbacks to the PAYE plan. First, you'll pay more interest than you would under the Standard Plan. That's because you'll be repaying the loan for 20 years rather than the Standard Repayment plan's 10 years. Second, you must reapply each year for the PAYE plan. Third, any balance forgiven after 20 years may be treated as taxable income.

There are four eligibility requirements for the PAYE plan.

1. You must have the right loan;
2. You must have gotten your first loan after 30 September 2007;
3. You must have gotten a loan disbursement after 30 September 2011; and
4. You must have a partial financial hardship.

You have the right loan if your loan isn't in default and is something other than:

- A PLUS Loan made to a parent;
- A Direction Consolidation Loan that includes a Parent PLUS loans; and
- An Unconsolidated FFEL and Federal Perkins Loan.

You meet the second and third requirements if (a) you borrowed a student loan for the first time during the 2008–09 school year and (b) you were still in school during the 2011–12 school year.

And you have a partial financial hardship if your annual loan repayment under the Standard plan is greater than the annual repayment you'd make under the PAYE plan. Typically, higher income borrowers have difficulty meeting this hardship standard unless they have high student loan balances.

- ◆ Use the income driven repayment application to apply for the PAYE plan. Send the application and proof of your income (typically your tax return) to each student loan servicer that has loans you can pay under the PAYE plan.

- ◆ On 9 June 2014, the President issued a memorandum directing the Department of Education expand the PAYE plan to additional Direct Loan borrowers. The memorandum isn't clear which additional borrowers will be affected. Whatever changes there will be are expected to occur before the end of 2015.

Income-Based-Repayment

In 2009, the government began offering the IBR plan. When originally launched, that plan capped all borrower's payments under the plan at 15% of their discretionary income and forgave the balance that remained after a borrower made 25 years of payments. That plan was later strengthened by capping new borrowers' payments at 10% and cutting their time for forgiveness from 25 years to 20 years of payments. (You're a new borrower if you got your first loan disbursement as of 1 July 2014.)

Besides capping the payment amount and forgiving the balance at 20 or 25 years, the IBR plan also benefits you by limiting the capitalization of your interest for the first three years of repayment.

The drawbacks of the IBR plan are the same as they are for the PAYE plan: you'll pay more in interest; you'll have to apply each year; and you'll likely pay taxes on the amount forgiven.

You're eligible for the IBR plan if you have (a) a partial financial hardship and (b) a Direct Loan or FFEL Loan. Two follow up points to those requirements. First, as is true with the PAYE plan, you have a partial financial hardship if your payment under the Standard plan would be greater than your payment under the IBR plan. Second, a loan that's in default and a Direct Consolidation Loan that repaid a Parent PLUS Loan aren't eligible for repayment under the IBR plan.

Borrowers who attended graduate school benefit the most under the IBR plan. That's because a graduate student can rack up a high federal student loan balance and then repay his student loans under the IBR plan and make low payments for several years and have his balance forgiven.

- The IBR plan has been criticized for its economic implications. Seemingly in response to that criticism, the Department of Education's fiscal year 2015 budget proposal suggested reform to student loan repayment, including the IBR plan. (The student loan reform proposal starts at page S-13 of the proposal.) Despite the Department's proposed reform efforts, some still argue more needs to be done.

- What does all that mean for you if you're already in repayment? I'm not sure. Student loan gurus Bill Penn and Heather Jarvis believe those already in repayment and those in school will continue to use existing repayment plans under the same or similar terms.

Income-Contingent-Repayment

Of the income-driven-repayment plans, the ICR plan is the oldest. Launched in the early 90's, the ICR plan, which requires repayment for 25 years, was designed to benefit low income borrowers and borrowers wanting to pursue public service careers. Under the ICR plan, monthly payments are capped at 20% of your discretionary income.

The benefits of the ICR plan are that:

- You don't have to have a partial financial hardship to qualify for the plan;
- Your capitalized interest is capped at 10% of the loan amount;
- Your remaining loan balance is forgiven after you've made 25 years of payments; and
- Unlike the PAYE and IBR plans, your Direct Consolidation Loan that repaid a Parent PLUS Loan or a Perkins Loan (or both), and your Graduate PLUS Loan qualify for repayment under the ICR plan.

The drawbacks of the ICR plan are the same as they are for the PAYE and the IBR plan: you'll pay more in interest; you'll have to apply each year; and you'll likely pay taxes on the amount that's forgiven. And in addition to those three, there's a fourth: there's no interest subsidy for the first three years of repayment under the plan.

Repayment plan extras

Calculating payment under PAYE and IBR. Under the PAYE and IBR plans your payment is calculated by taking 15% (or by 10% for PAYE and some IBR plan borrowers) of your discretionary income. To find your discretionary income, subtract 150% of the poverty guideline for your family size and location from your adjusted gross income. The remaining amount is your annual discretionary income. Once you have that amount, multiply it by 15% (or if you're a new borrower, 10%) and then divide that amount by 12. That final number is your monthly payment amount under the PAYE plan or the IBR plan.

Calculating payment under ICR. Under the ICR plan, your payment is the lesser of 20% of (a) your discretionary income (use the same formula as you would for the PAYE or IBR plans) or (b) what you would pay on a repayment plan with a fixed payment over 12 years, adjusted to your income. Instead of doing the math yourself, use the Repayment Estimator at studentloans.gov.

Proof of income under IDR plans. Provide a copy of your tax return from this year or last as proof of your income. You may need to provide alternative proof if you haven't filed a tax return in the past two years or if last year's AGI differs significantly from what you're earning now. If you have to provide alternative proof, provide a pay stub or other proof of your income such as (1) a letter from your employer listing your income; (2) a copy of your interest or bank statement; (3) a copy of your dividend statements; or (4) a letter from you explaining the source of your income and giving the name and address of the source. And if you have no income, indicate that on your application.

You can have a zero dollar payment. Under the income driven repayment plans, your monthly payment may be zero. A zero dollar payment counts towards forgiveness under the repayment plans and under the Public Service Loan Forgiveness program.

You can have nonconsecutive payments. To qualify for term forgiveness (that is, forgiveness at 20 or 25 years) under the income-driven-repayment plans, your payments don't have to be consecutive. You just have to make 20 or 25 years of payment. So if you take 30 years to make 25 years of payment, so be it.

Tax issues after forgiveness. After you've made 20 or 25 years of payments under the particular income driven repayment plan and you're eligible for forgiveness, the IRS will treat the forgiven amount as taxable income. You may have that forgiven amount excluded from your taxable income depending on your situation. Speak with a tax professional to learn more about this exclusion

You have to recertify annually. Under the income-driven-repayment plans you have to recertify your income and family size annually. This should happen within 35 days of the date you certified the year before. You're supposed to get a reminder to recertify within 60–90 days of your anniversary date. If you don't recertify your income, your monthly payment will jump to what it would be under the Standard plan. And if you don't certify your family size, your family size will be one for that year.

Mid-year changes in your income. If you lost your job or if your salary decreased after you certified your income, submit proof of your job or salary loss so your payment can be recalculated.

Proof of income. Since income-driven-repayment plans are based on your income, you have to provide proof of what your income is. Most borrowers provide a copy of their previous year's tax return, which shows their adjusted gross income for that year. If your AGI doesn't reflect what you're currently making, you must submit additional proof of your income. Typically, this can be a recent pay stub or a letter from your employer stating how much you earn and how often you're paid.

Joint consolidation loans. If you and your current (or former spouse) have a joint consolidation loan, you may repay under the IBR plan if both of you have a partial financial hardship.

Married couples payment. Your spouse's income will be considered under the income-driven-repayment plans if you file taxes jointly. But if you file separately, only your AGI will be considered. And if you want, you and your spouse may repay your student loan bills together. I don't know why you and bae would do that. (Side note: I hate the term "bae" for these four reasons: http://wapo.st/1NYWMmz.) But you might. So just know that you can make your payment together. If you ever want to stop paying together, resubmit an income-driven-repayment application requesting that separation.

Same-sex married couples. If your spouse is the same sex as you, you're considered married for income-driven-repayment purposes if you got married in a jurisdiction that recognizes same sex marriages. And that remains true even if you no longer live in that jurisdiction. The Department of Education calls this the "place of celebration" rule.

No longer have a partial financial hardship. You may stay in your PAYE or IBR plan even if you no longer have a partial financial hardship or no longer want to make payments based on your income. When that happens, your payments won't exceed what you would've paid under the Standard plan when you first entered the PAYE or IBR plan.

Switching plans. If you're in the PAYE, IBR, or ICR plans, you may change your repayment plan to any other repayment plan. Except if you're in the IBR plan, you must first make one payment under the Standard plan before switching to another repayment plan.