You have CHOICES

Decisions to be made ...

- Should you pay the interest on your loans as it is accruing in school?
- Should you refinance your federal loans with a private loan to get a lower interest rate?
- Should you consolidate your federal loans in the Federal Consolidation Loan program?
- What payment plan should you choose to repay your federal student loans?
- Should you pay off your federal student loans as fast as possible?
Majority of law students ...

... now graduate with an EDUCATIONAL MORTGAGE
Essentially, you’re financing an important investment in yourself

You can be successful …

- In repaying this “mortgage”
- Without having to sacrifice your career aspirations or the achievement of your other financial and personal goals

But, you must make **smart, strategic, and well-informed** decisions about how you plan for and manage repayment of your federal student loans!
Normally with debt ... 

... you’re “boxed into a corner” from a financial perspective!
Why are you in that “corner”? 

- Because payments are based on the amount you owe—your DEBT—not on your ability to repay that debt. 

- Your monthly payment is equal to the amount required to pay off all the debt (plus interest) in a given period of time.

You must make that payment each and every month whether you can afford it or not!
Debt puts you at risk and limits your options, financially

*In other words, it “boxes you into that corner”*

- Puts you at risk of having to miss the payment (e.g., *due to loss of income or unexpected expense*)

  - *Missing the payment will damage your credit!*

- Impacts your ability to make other choices financially (e.g., *changing jobs or taking time off, investing for retirement, buying a house*)

  - *The more you owe, the more you must pay each month on your debt leaving less money for other purposes!*
With federal student loans...

... you don’t need to be “boxed” into that corner!
Federal student loans offer ... Choice Flexibility Safety
How are federal student loans different?

The **IMPORTANT** difference:

- Payments can be based on your **income** rather than on the **amount of your debt**
- Payments can be equal to **10%** of your **household’s discretionary income** – therefore, you could have **90%** of your household’s income for everything else!

As such, federal student loans need not “**box you into a corner financially**” – you have options!
Making informed decisions ...

... also requires understanding the total "cost" of debt
Debt always has two (2) costs ...

- **Direct Cost**
  - Interest
  - Fees

- **Opportunity Cost**
  - Value of what you are forgoing to repay the debt
Another factor to consider ...

**Simple vs. Compounding Interest**

- **Simple interest**
  - Increases in a **LINEAR** manner over time because it is not being “capitalized” (*not being added to the principal balance*)
  - Interest generally accrues on your federal student loans as “**SIMPLE**” interest during repayment

- **Compound interest**
  - Increases **EXPONENTIALLY** over time because it is being capitalized (added to the principal balance)
  - Interest is compounding (perhaps as often as daily) on your **INVESTMENTS** and so your money is GROWING exponentially!

As such, you could end up with more money (not less) by investing your extra funds rather than paying off your federal loans faster!
So what should you do ...

... *when “mapping your course” for loan repayment?*
Remember, you have decisions to be make ...

- Should you pay the interest on your loans as it is accruing in school?
- Should you refinance your federal loans with a private loan to get a lower interest rate?
- Should you consolidate your federal loans in the Federal Consolidation Loan program?
- What payment plan should you choose to repay your federal student loans?
- Should you pay off your federal student loans as fast as possible?
Should you pay the interest while it accrues in school?

*Interest on unsubsidized federal loans accrues as **SIMPLE** interest while in school!*

- It is **NOT** compounding while you are in school!
- Interest that accrues while you are in school **“capitalizes”** only when loan(s) enter/re-enter repayment.

*Therefore, it is better to reduce amount you are borrowing rather than paying the accruing interest if you have funds to pay that interest while in school—you will get more “**bang for your buck**!”*
Did you know?

You can return unused loan funds!

If you return loan funds within 120 days of disbursement:

- Total amount owed is reduced
- Interest and fees charged on loan amount returned are reversed

Contact the financial aid staff for more information.
Should you refinance with a private loan?

You have the right to do so, BUT:

- You will lose the choice, flexibility and safety provided by federal student loans including the income-driven repayment options.

- You may lower the direct cost, but will increase the opportunity cost (likely will have to repay the private loan faster, and therefore, have a higher monthly payment to qualify for the lower interest rate).

As such, you may be giving up more than you are gaining if you borrow a private loan – so exercise caution – be fully informed – investigate ALL the differences -- don’t focus solely on the interest rate!
Should you “consolidate” your federal student loans?

- May be helpful – particularly if you have non-DIRECT federal student loans – not likely necessary if you only have DIRECT Loans

- **Consolidation** is the *refinancing* of federal student loan debt—not the *combining* of debt—you are borrowing a *new Federal Direct Consolidation Loan*

- Only *federal* student loans are eligible

- Does **NOT** lower the cost of the debt
  - Interest rate is *fixed*--equals weighted average of interest rates of loans being consolidated, but then it is *rounded up to nearest 1/8th percent*
What payment plan should you choose?

Consider:

- Choosing the payment plan that offers the **LOWEST** scheduled monthly payment – you can always pay extra

Why?

- This provides *maximum cash flow flexibility* so that you can:
  - Maximize amount you are prepaying in a targeted way at your most expensive debt (e.g., credit cards, private student loans)
  - AND/OR
  - Allocate “extra cash” for other purposes (e.g., investing and saving for the future)
Should you pay off your federal loans as fast as possible?

You have the right to do so—there are no prepayment penalties.

- But, faster may not be better when repaying your federal student loans.

You may want to consider:

- Taking as long as possible to repay your Federal Student Loans.

Why?

- You may have better uses for your “extra” funds in terms of “opportunity cost.”
How will you use your money?

You must decide how to allocate your money across four "buckets" ...

- **Past**: Debts
- **Present**: Living expenses
- **Future**: Savings, investments
- **Philanthropy**: Charitable donations
The “Future” Bucket …
A “bucket” you’ve been ignoring!

Financial planners suggest you should “Pay Yourself FIRST” using at least 20% of your gross monthly income on …

- Saving for a “rainy day” – the emergency fund
  - Minimum of 6-9 months of your monthly living expenses

- Investing for retirement
  - Minimum of 10% of your gross monthly income

- Saving for their children’s education
  - Minimum needed uncertain—may need to start paying for children’s education much sooner than expected (e.g., elementary school)

- Saving for the down payment/closing costs for a home
  - Minimum of 10% of purchase price
Paying off your federal student loans faster ...

- **Reduces** the **Direct Cost** by lowering total interest expense on the debt

- **BUT, it simultaneously**

- **Increases** the **Opportunity Cost** because it diverts more of your current income from investing/saving in the “**FUTURE** bucket”

*Therefore, when repaying your federal student loans, you need to evaluate this tradeoff between the **DIRECT** and **OPPORTUNITY** costs as well as the difference in **SIMPLE** vs. **COMPOUNDING** interest so that you make an informed decision that meets all your financial needs!*
Loan Repayment Options
Plans fall into two (2) categories

<table>
<thead>
<tr>
<th>Original Plans</th>
<th>Newest Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment based on amount of <strong>DEBT</strong></td>
<td>Payment based on <strong>INCOME</strong></td>
</tr>
<tr>
<td><strong>Plans</strong></td>
<td><strong>Plans</strong></td>
</tr>
<tr>
<td>Standard</td>
<td>Revised Pay As You Earn (REPAYE)</td>
</tr>
<tr>
<td>Graduated</td>
<td>Pay As You Earn (PAYE)</td>
</tr>
<tr>
<td>Extended <em>(fixed)</em></td>
<td>Income-Based Repayment (IBR) – 2 options</td>
</tr>
<tr>
<td>Extended <em>(graduated)</em></td>
<td>Income-Contingent Repayment (ICR)</td>
</tr>
</tbody>
</table>
Amortization Schedule

Payments Based on DEBT

- Schedule of monthly payments (installments) that is based on:
  - Amount of debt
  - Interest rate
  - Length of repayment term

- Fundamentally, it represents the amount you must pay each month to fully repay the debt and all accrued interest by the end of the repayment term
## Payment Plans

**Payments Based on DEBT**

<table>
<thead>
<tr>
<th>Plans</th>
<th>Payment Structure</th>
<th>Term</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Standard (default plan)</strong></td>
<td>Fixed payments <em>(do not change)</em></td>
<td>10 years*</td>
</tr>
<tr>
<td></td>
<td></td>
<td><em>(up to 30 years on Consolidation Loans)</em></td>
</tr>
<tr>
<td><strong>Graduated</strong></td>
<td>Payments increase in graduated steps every 2 years</td>
<td>10 years*</td>
</tr>
<tr>
<td></td>
<td></td>
<td><em>(up to 30 years on Consolidation Loans)</em></td>
</tr>
<tr>
<td><em><em>Extended</em> (fixed)</em>*</td>
<td>Fixed payments <em>(do not change)</em></td>
<td>25 years</td>
</tr>
<tr>
<td><em><em>Extended</em> (graduated)</em>*</td>
<td>Payments increase in graduated steps every 2 years</td>
<td>25 years</td>
</tr>
<tr>
<td></td>
<td><em>Interest-only payments for first 2 years</em></td>
<td></td>
</tr>
</tbody>
</table>

- Payments are based on an *amortization schedule* – *must fully repay all the debt in the term of the loan (maximum payment period)*
- Monthly payment must at least equal the accrued interest each month—*negative amortization* is NOT permitted in these plans
- * Must have more than $30,000 in Direct Loans to use EXTENDED plans
Income-Driven Repayment (IDR)

Payments Based on INCOME

- Fundamentally, payments are based on a percentage of your household’s “DISCRETIONARY” income—not on the amount of your debt.

- Payments are adjusted every 12 months based on how your income and family size change.

- Monthly payments can be less than the accrued interest each month ("negative amortization" is permitted).
“Discretionary Income”

DISCRETIONARY INCOME:

Portion of your household’s Adjusted Gross Income (AGI) that exceeds 150% of federal poverty guideline for your family size and state of residence

HOUSEHOLD’S ADJUSTED GROSS INCOME (AGI):

If single:
- Only your Adjusted Gross Income (AGI)

If married:
- REPAYE – includes both your AGI and spouse’s AGI regardless of how you file your federal tax return
- PAYE/IBR – only includes both your AGI and your spouse’s AGI if you file a JOINT federal tax return (excludes spouse’s AGI if you file separate federal tax returns)

NOTE: IDR payment calculation will take into account spouse’s eligible debt if spouse’s AGI is included
## Payment Plans

**Payments Based on INCOME**

<table>
<thead>
<tr>
<th>Plans</th>
<th>% of Disc. Income</th>
<th>New Borrower</th>
<th>PFH Required</th>
<th>Forgiveness (taxable benefit)</th>
<th>Subsidy</th>
</tr>
</thead>
<tbody>
<tr>
<td>REPAYE*</td>
<td>10%</td>
<td>NO</td>
<td>NO</td>
<td>20/25 yrs (UG only/UG&amp;Grad)</td>
<td>All loans (No time limit)</td>
</tr>
<tr>
<td>PAYE*</td>
<td>10%</td>
<td>YES</td>
<td>YES</td>
<td>20 yrs</td>
<td>Sub. only (up to 3 yrs)</td>
</tr>
<tr>
<td><strong>IBR for New Borrowers</strong></td>
<td>10%</td>
<td>YES</td>
<td>YES (payment capped)</td>
<td>20 yrs</td>
<td>Sub. only (up to 3 yrs)</td>
</tr>
<tr>
<td>IBR</td>
<td>15%</td>
<td>NO</td>
<td>YES (payment capped)</td>
<td>25 yrs</td>
<td>Sub. only (up to 3 yrs)</td>
</tr>
<tr>
<td>ICR*</td>
<td>20%</td>
<td>NO</td>
<td>NO</td>
<td>25 yrs</td>
<td>NO</td>
</tr>
</tbody>
</table>

* Only Federal DIRECT Loans are eligible for this plan *(FFEL loans must be consolidated to be eligible for REPAYE, PAYE and ICR)*
# Interest Subsidy

**Subsidy during “negative amortization”**

<table>
<thead>
<tr>
<th>Plans</th>
<th>Subsidized Loans</th>
<th>Unsubsidized Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>REPAYE</strong></td>
<td>100% of negative amortization during first 3 years in plan; <strong>50% thereafter</strong></td>
<td><strong>50% of negative amortization during all years in plan</strong></td>
</tr>
<tr>
<td><strong>PAYE</strong></td>
<td>100% of negative amortization during first 3 years in plan; none thereafter</td>
<td>NONE</td>
</tr>
<tr>
<td><strong>IBR</strong> for New Borrowers</td>
<td>100% of negative amortization during first 3 years in plan; none thereafter</td>
<td>NONE</td>
</tr>
<tr>
<td><strong>IBR</strong></td>
<td>100% of negative amortization during first 3 years in plan; none thereafter</td>
<td>NONE</td>
</tr>
<tr>
<td><strong>ICR</strong></td>
<td>NONE</td>
<td>NONE</td>
</tr>
</tbody>
</table>
To “Log In” enter your FSA ID:
- Username
- Password

Then select the “Repayment Estimator” from the tools and calculators that are available on the Welcome Screen.
## Sample Monthly Payments

**Assumed Amount Owed = $110,000**  
**Assumed Interest Rate = 6.2%**

<table>
<thead>
<tr>
<th>Plans</th>
<th>AGI $40,000</th>
<th>AGI $65,000</th>
<th>AGI $160,000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Standard (10 yrs)</strong></td>
<td></td>
<td></td>
<td><strong>ALL = $1,232</strong></td>
</tr>
<tr>
<td><strong>Graduated (10 yrs)</strong></td>
<td></td>
<td><strong>1st = $706</strong></td>
<td><strong>120th = $2,119</strong></td>
</tr>
<tr>
<td><strong>Extended Fixed (25 yrs)</strong></td>
<td></td>
<td></td>
<td><strong>ALL = $722</strong></td>
</tr>
<tr>
<td><strong>Extended Graduated (25 yrs)</strong></td>
<td></td>
<td><strong>1st = $568 (interest only)</strong></td>
<td><strong>300th = $1,072</strong></td>
</tr>
<tr>
<td><strong>REPAYE (10%)</strong></td>
<td><strong>1st = $183</strong></td>
<td><strong>1st = $391</strong></td>
<td><strong>1st = $1,183</strong></td>
</tr>
<tr>
<td></td>
<td><strong>300th = $809</strong></td>
<td><strong>296th = $1,481</strong></td>
<td><strong>100th = $1,788</strong></td>
</tr>
<tr>
<td><strong>PAYE (10%)/IBR for NEW Borrowers (10%)</strong></td>
<td><strong>1st = $183</strong></td>
<td><strong>1st = $391</strong></td>
<td><strong>1st = $1,183</strong></td>
</tr>
<tr>
<td></td>
<td><strong>240th = $606</strong></td>
<td><strong>240th = $1,133</strong></td>
<td><strong>121st = $1,232</strong></td>
</tr>
<tr>
<td><strong>IBR (15%)</strong></td>
<td><strong>1st = $274</strong></td>
<td><strong>1st = $586</strong></td>
<td>Not eligible</td>
</tr>
<tr>
<td></td>
<td><strong>300th = $1,214</strong></td>
<td><strong>206th = $1,232</strong></td>
<td>(no PFH)</td>
</tr>
</tbody>
</table>
**Interest Subsidy—**REPAYE

Federal Student Loan Debt = $110,000 (all unsub) *(Weighted avg. interest rate = 6.2%)*

Household AGI = see below *(Household Size = 1; State = MA; 2017 Poverty Guidelines)* *(Estimates calculated using “Repayment Estimator” at: StudentLoans.gov)*

<table>
<thead>
<tr>
<th>Item</th>
<th>AGI = $40,000</th>
<th>AGI = $65,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest accrued/month</td>
<td>$568</td>
<td>$568</td>
</tr>
<tr>
<td><em>(“Extended Graduated” plan)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>“REPAYE” monthly payment</td>
<td>$183</td>
<td>$391</td>
</tr>
<tr>
<td>Negative amortization (unpaid interest)</td>
<td>$385</td>
<td>$177</td>
</tr>
<tr>
<td>50% subsidy of negative amortization</td>
<td><strong>$192.50</strong></td>
<td><strong>$88.50</strong></td>
</tr>
<tr>
<td>Annual subsidy</td>
<td>$2,310</td>
<td>$1,062</td>
</tr>
</tbody>
</table>
To apply for an IDR plan, click on: “Apply for an Income-Driven Repayment Plan”
Completing IDR Plan Request

The “Loophole” Question

- Step 2 of the IDR application asks the following question:
  - “Has your income *changed significantly* from the AGI on your prior year’s federal tax return, for example have you lost your job or had a loss of income?”

- “*Changed Significantly*” is not defined—*that is the “loophole”*
  - The only clarification is the example: “... *have you lost your job or had a loss of income?”*
  - As such, there is no wrong answer to the question—you can answer **NO** even if you now have **more income**

*BUT, you must file your tax return for the prior year to take advantage of this “loophole”*
Be strategic in repayment ...

... leverage the unique nature of federal student loans!
Direct Loan payment tips ...

- **SINGLE statement billing**
  - You should receive a “combined/itemized/consolidated” monthly bill and have one monthly payment for your DIRECT Loans

- **Payments can be made using:**
  - Check or money order
  - Online electronic payment at loan servicer’s website
  - **“Auto-Pay”** *(contact your loan servicer to apply)*
    - Saves time
    - Saves money -- *interest rate reduced by 0.25%*
For more information ...

- Contact your loan servicer(s)

- Online resources:
  - Federal student loan repayment: StudentAid.gov
  - Federal loan “Repayment Estimator”: StudentLoans.gov
  - Federal Direct Consolidation Loans: StudentLoans.gov
  - Income-Driven Repayment (IDR) Plans: StudentLoans.gov
  - National Student Loan Data System: NSLDS.ed.gov
  - Public Service Loan Forgiveness Program (PSLF):
    - Online at: StudentAid.ed.gov/PublicService
    - Call Fedloan Servicing at: 1-855-265-4038
  - Free annual credit report: AnnualCreditReport.com
BE STRATEGIC:
Take Charge of Loan Repayment!

Jeffrey Hanson
Education Services

Boston University School of Law