

Grads neck-deep in debt have options

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USA TODAY, in partnership with ABC News, is exploring the issues of being young and in debt in a six-week series that began Monday, Nov. 20. We've paired five twentysomethings with members of the Financial Planning Association who are lending advice. And we're offering tips for managing debt, cutting expenses and saving. Follow the entire series and find online tools and resources at youngdebt.usatoday.com.

By Sandra Block, USA TODAY

If your student loans loom large now, just try ignoring them. They'll get much, much bigger.

Once your loans go into default, your lender would probably turn your account over to a collection agency. The agency's fees would be added to the balance, increasing the amount you owe. The government might also withhold your tax refund and garnish some of your wages.

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And unlike with most other debts, there's no statute of limitations on the government's authority to pursue unpaid student loans, says Deanne Loonin, staff attorney for the National Consumer Law Center. "That means these debts can follow you your whole life."

The encouraging news is that these unfortunate consequences are avoidable. The federal loan program offers numerous alternatives for borrowers who can't afford their monthly payments. To take advantage of them, you need to contact your lender as soon as you run into trouble.

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You're required to start making payments on your student loans at the end of your grace period, typically six months after you graduate or leave school. In most cases, your lender will send you a repayment schedule near the end of your grace period. But you're responsible for making your payments even if you don't receive a notice. So if you move, make sure your lender knows where you are.

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Your lender's schedule of monthly payments will be based on the standard repayment plan; it gives you 10 years to repay your loan. The standard plan requires larger monthly payments than do programs that let you stretch out the term of your loan. But because you'll repay your loan more quickly, you'll pay less in interest than with the other plans.

Payment options

If you can't afford the monthly payments under the standard plan, talk to your lender about other repayment programs. The most

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common repayment plans are:

•**Extended repayment.** This will lengthen the term of your loan to up to 25 years. To qualify, you must owe at least \$30,000. Your payments will be lower, but you'll pay more in interest. There's no penalty, though, for paying off your loans early, so you can always increase your payments once you start earning more income.

•**Graduated repayment.** This plan lets you make interest-only payments for up to four years. After that, your payments will rise gradually so your loan will be repaid in 10 years.

•**Income-sensitive repayment.** Your monthly payment will be based on your income and the amount you owe. Borrowers must apply annually for this option and are usually asked to provide copies of tax returns and W-2 forms. Your payments must be large enough to cover the interest on your loan. For Federal Family Education Loans (see box), income-sensitive payments are limited to five years; after that, your payments will be based on a 10-year, standard repayment term. Because payments could increase significantly after the first five years, this plan is most appropriate for borrowers who expect their income to increase — or their expenses to decline — in the next few years.

•**Loan consolidation.** This is worth considering if you have several federal loans. You can combine them into a single loan and extend the term for up to 30 years, depending on the amount you owe.

When federal loan interest rates were variable, borrowers could lock in a low rate by consolidating their loans. But a law enacted last year established a fixed rate of 6.8% for loans issued after July 1, eliminating that benefit of consolidation.

Still, consolidation is smart for many students, says Robert Franek, vice president at Princeton Review, which publishes college guides. By combining your loans, he says, you don't have to worry about overlooking a payment.

When you can't pay

If you can't afford your loan payments, even with a longer-term or income-sensitive plan, don't flee the country. There are alternatives. The two most common:

•**Loan deferment.** Borrowers who return to college, are unemployed or are suffering from economic hardship may defer repaying their loans for up to three years. Interest on Perkins loans and subsidized Stafford loans, which go to students with financial need, won't accrue during the deferment period. Interest on unsubsidized Stafford loans, available to all students, will accrue during deferment.

Lenders are required to grant deferment to eligible borrowers. You'll have to fill out a form and may need to provide documents supporting your case.

•**Forbearance.** This also lets borrowers temporarily stop payments, or pay a reduced amount. Forbearance is granted at the discretion of the lender, but the standards aren't as strict as those for deferment, says Paul Combe of American Student Assistance, a company that helps borrowers manage their loans. Having a lot of credit card debt, for example, won't qualify you for a deferment, but you may get forbearance, Combe says.

INS AND OUTS OF STUDENT LOANS, REDUCING INTEREST

Types of student loans:

If you're having trouble tracking down your student loans, your college financial aid office might be able to help. You can also get information about your federal student loans at the National Student Loan Data System, www.nslds.ed.gov.

Federal Family Education Loan Program loans. These loans are provided by private lenders and are guaranteed by the federal government. Most Stafford loans are FFELP loans.

Federal Direct Student Loan Program loans. These loans are provided by the U.S. government directly to students. For more information, go to www.ed.gov/directloan.

Private student loans. These loans are often issued by the same lenders that provide FFELP loans, but they're not guaranteed by the federal government. Interest rates on these loans are usually variable. In addition, private lenders aren't required to offer the same repayment options available under the federal student loan program. For information about these loans, contact the lender.

How to reduce the amount of interest on

your student loans:

Arrange for automatic withdrawal from a checking or savings account. Most lenders will reduce your interest rate by a quarter of a percentage point if you arrange for automatic withdrawal.

Pay on time. Many lenders offer another rate reduction for borrowers who make a specific number of on-time payments. Some lenders will reduce your rate by up to 1 percentage point.

In addition, make sure you take advantage of the tax deduction for student loan interest.

Eligible taxpayers can deduct up to \$2,500 in student loan interest a year.

This is an above-the-line deduction, so you don't have to itemize to claim it.

The biggest drawback to forbearance: Interest will accrue on the loan, no matter what kind of loan you have. That will increase the amount you owe when you emerge from forbearance. For this reason, Combe says, "Forbearance should be seen as a last resort."

It's important to continue making payments until your request for deferment or forbearance is granted. If you fail to make your payments for nine months, your loan will be declared in default, and you'll be ineligible for either form of relief.

"A borrower working in good faith should have no reason to default as long as they stay in touch," Combe says. "When they get in trouble is when they start hiding."

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