Shrinking Student Loans

Daniel Ward explains how teachers can combine student loan repayment programs to minimize qualification costs

The Income-Based Repayment (IBR) plan, part of the College Cost Reduction and Access Act of 2007, becomes available at the beginning of this month, giving college graduates a new option in paying off their student loans that will cap monthly payments based on income. It targets borrowers who would have a hard time paying basic living expenses if they had to make standard monthly payments on their loans. Teachers can use it in conjunction with the Public Service Loan Forgiveness program to significantly and legitimately reduce their total loan repayment.

Under the income-based repayment program, borrowers will never have to spend more than 15 percent of their discretionary income — an amount based on federal poverty guidelines — on student loan payments. Most who qualify for the program will not spend more than 10 percent of their income on student loans. Those whose income falls below 150 percent of the poverty level will not have to make any payments.

How the new program works:

Suppose you have $30,000 in student loans, and you estimate that your 2009 income will be $25,000. Assuming your loans have a fixed interest rate of 6.8 percent, your monthly payment under the income-based repayment program would be $110, vs. $345 under a standard 10-year repayment plan.

If your income rises in the future, your payments will, too.

Unfortunately, not all students are eligible to participate in the income-based repayment plan, even if they're experiencing economic hardship.

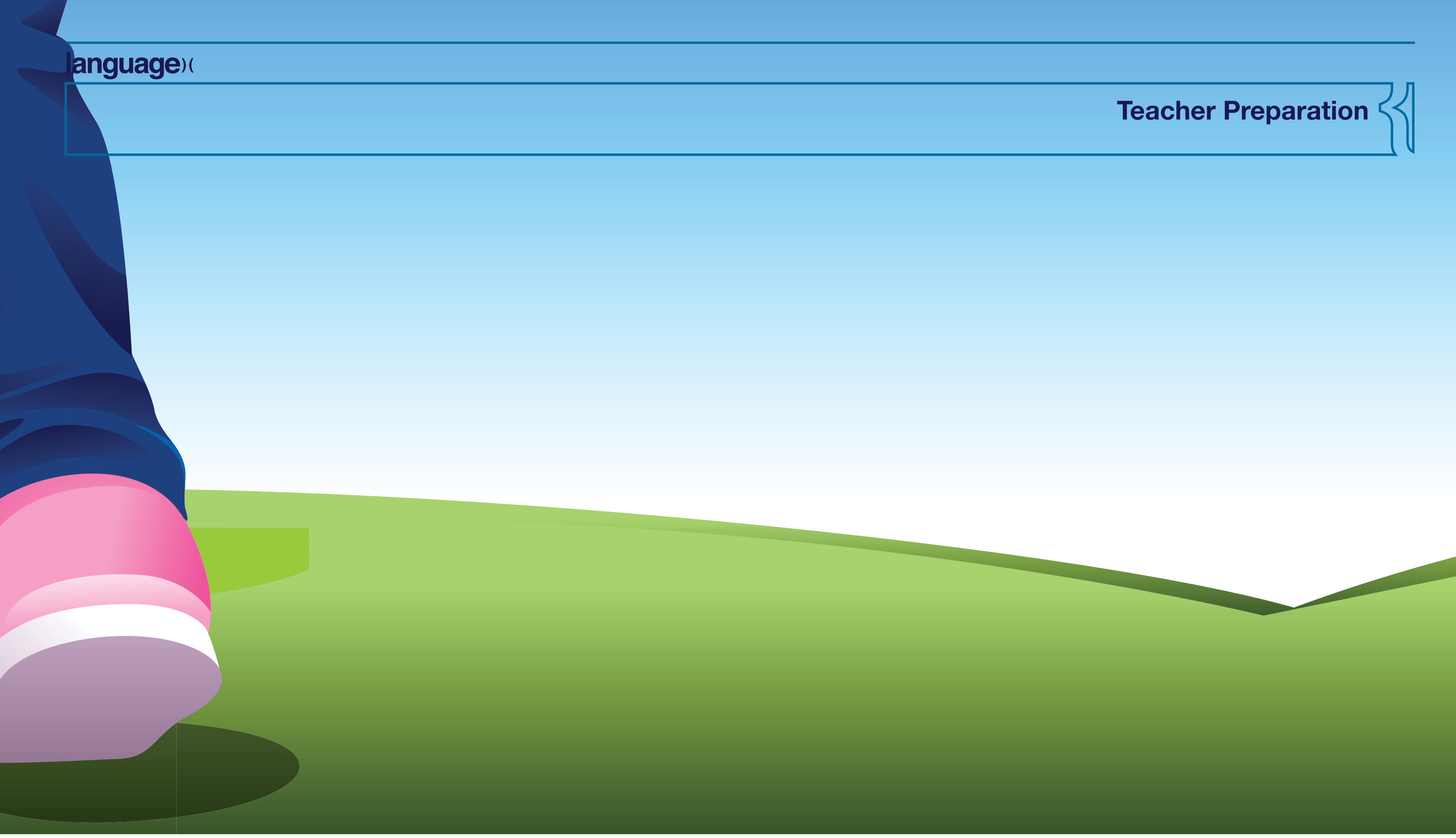
You are ineligible if:

- You have private student loans. The income-based repayment program is limited to federal Stafford, Grad Plus and federal consolidated loans. Limits on federal student loans were increased last year, so make sure you take full advantage of these loans before venturing into the private market.
- You have defaulted on your student loans. The income-based repayment program is available for all federal student loans, no matter when you took them out, but you must be in good standing to qualify. Most student loans are considered in default after you have failed to make payments for nine months.

To enroll in the income-based repayment program, you'll need to contact your lender. The Project on Student Debt has set up a website with information and updates about the program. Find it at www.ibrinfo.org.

For some borrowers, the reduced payments will not cover the interest on their loans. For those with subsidized Stafford loans — which are provided to students who demonstrate economic hardship — the government will pay the interest for the first three years of the program. For unsubsidized loans, the interest will be added to the balance, so you could come out of the program with a larger loan balance.

However, any amount you owe after 10 years of qualifying payments will be forgiven under the Public Service Loan Forgiveness program for federal student loan borrowers who work in certain kinds of jobs, like teaching. It will forgive remaining debt after 10 years of eligible employment and qualifying loan payments. This is significant because, in the past, it was nearly impossible for borrowers to get out from under their student loan debts. Under cur-



rent bankruptcy laws, borrowers must demonstrate "undue hardship" before a bankruptcy court will discharge a student loan, a costly and difficult standard to meet.

Who qualifies for Public Service Loan Forgiveness?

This program is for people with federal student loans who work in a wide range of "public service" jobs, including jobs in government and nonprofit 501(c)(3) organizations.

What are eligible jobs? In most cases, eligibility is based on whether you work for an eligible employer. Your job is eligible if you:

- Are employed by the federal government, a state government, local government, or tribal government (this includes public schools and colleges and the military); or
- Are employed by any nonprofit, tax-exempt 501(c)(3) organization; or
- Serve in a full-time AmeriCorps or Peace Corps position.

If you don't meet these criteria, the Department of Education's regulations create a two-part test of other circumstances under which you may still be eligible:

1 Your employer is not "a business organized for profit, a labor union, a partisan political organization, or an organization engaged in religious activities, unless the qualifying activities are unrelated to religious instruction, worship services, or any form of proselytizing;" and,

2 Your employer provides any of the following public services: early childhood education; public education; public library services; and school library or other school-based services; emergency management; military service; public safety; law enforcement; public interest law services; public service for individuals with disabilities and the elderly or public health;.

These definitions of eligible jobs reflect the Department of Education's final regulations for PSLF, as posted in the Federal Register on October 23, 2008.

What kinds of loans does it cover?

It covers federal Stafford, Grad PLUS, or consolidation loans as long as they are in the Direct Loan program. Borrowers with loans in the Guaranteed (or FFEL) loan program must switch to the Direct Loan program to get this benefit.

When does the 10-year clock start, and which payments count? Only payments made after October 1, 2007 count towards the 10 years (120 monthly payments, not necessarily consecutive) required for Public Service Loan Forgiveness. Qualifying payments must be made through the Direct Loan program and include Income Contingent Repayment, Standard (10-year) Repayment, or Income-Based Repayment (available in July 2009).

To count, these payments must be made while you're working full-time in an eligible job. "Full-time," according to the final regulations issued by the Department of Education, means an annual average of 30 hours per week or the standard for full-time used by the employer, whichever is greater. For people working part-time at two or more qualifying jobs, "full-time" means an annual average of 30 hours across all jobs held. In professions such as teaching, annual contracts that include at least eight months of full-time work will be treated as the equivalent of a full year's employment. If you meet all the criteria, the earliest your remaining debt could be forgiven is October 2017.

What if I've already paid off my loans by then? This loan forgiveness program will only benefit people who still owe money on their federal loans after 10 years of eligible payments and employment. If your income is low relative to your debt, and you qualify for reduced payments under IBR at any time during those 10 years, you will likely have debt left to forgive.

For further information, consult a qualified financial advisor.

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