

# **COLLEGE LOANS - 2010**

## **Facts About College Loans**

**By**  
**Gary E. Carpenter, CPA**  
**Copyright 2010**

**Updated May 31, 2010**

# Gary E. Carpenter, CPA

## Biography

Gary Carpenter is a Certified Public Accountant (CPA) in New York and a Certified College Planning Specialist (CCPS). He is the owner of College Planning Services and co-founder of the CollegeLOAN Evaluator. Mr. Carpenter has also provided continuing education courses in the area of college planning and financial aid for various state CPA societies, the New York State Bar Association and the Financial Planning Association of New York. He is co-author of College Financial Planning for Any Income Level and has been quoted in *Kiplinger's Personal Finance*, *Washington Post*, *AARP Magazine*, *MONEY*, *Financial Advisor*, and on MSNBC and CNBC. He has had over thirty years experience in tax and financing and has spent the past eleven years in college planning and consulting. He is a member of the New York State Society of Certified Public Accountants, the American Institute of Certified Public Accountants and a co-founder and the Executive Director of the National College Advocacy Group. He is active in committee service for the New York State Society of CPAs and serves on the boards of several non-profit organizations.

Gary E. Carpenter, CPA

Telephone: 315-487-4567

E-mail address: [gec@collegeloanevaluator.com](mailto:gec@collegeloanevaluator.com)

As we enter 2010, families will see some major changes in the student loan environment. Many families do not realize that the Health Care Bill passed in March includes changes in federal student loans (“Health Care and Education Affordability Reconciliation Act of 2010”).

The most important change is the termination of one of the two Federal Student Loan programs. Effective July 1, 2010, the Federal Family Education Loan (FFEL) Program will be terminated and all federal student loans first disbursed after that date will be under the “William D. Ford Direct Loan Program” (Direct Loan Program). Loans that will be available under this program are:

1. Federal Stafford Loans (Subsidized and Unsubsidized)
2. Federal PLUS Loans
3. Federal Grad PLUS Loans

Presently, the Perkins Loan Program has not been affected by this change in the law. Institutions participating in the Title IV Federal Student Aid Program will continue to make the need-based Perkins Loans to their students. The institutions will loan the funds to students using their own resources and the federal government will guarantee those loans.

Private education loans continue to be harder to qualify for. These credit-based loans require a co-signer with a good credit score. Borrowers are also finding that these private education loans are hard, if not impossible, to consolidate after the student has left school.

I’m going to repeat myself now, but the most important thing a family should do after receiving award letters is to calculate how much each school is going to cost for the total four years. This cost figure is the total cost of attendance less any grants or scholarships multiplied by the number of expected years of college.

***Example***

TOTAL COST OF ATTENDANCE FOR ONE YEAR (includes tuition, fees, room & board, books personal expense, computer and transportation)	\$ 40,000
LESS GRANTS/SCHOLARSHIPS	<u>10,000</u>
AMOUNT TO BE PAID BY THE FAMILY	\$ 30,000
TIMES THE NUMBER OF YEARS OF COLLEGE	<u>x4</u>
TOTAL COLLEGE COST TO BE PAID	<u>\$120,000</u>

This number is an **estimate** and will increase each year with the rising college costs.

In any event, the family must look at the four year cost figure and determine how they will pay for it. Will it come from savings, their current earnings or will they borrow the funds?

If the family is thinking of borrowing for college, they need to ask themselves these questions:

1. Do we manage debt well? (Debt Discipline)
2. Can we afford college debt in addition to our current debt load? (Debt Capacity)
3. Do we have other children who will be going to college in the future? (Debt Load)
4. Who can borrow? (Qualified Borrower)
5. Who will borrow the money and how much will they borrow? (Borrower(s))

Once the family has answered these questions and if they decide to borrow for college, they need to review the loan options that are available to them.

Here is a short list of educational loans that may be available to the family:

1. Federal Stafford Loan (Subsidized and Unsubsidized)
2. Federal Perkins Loan (Need Based Loan)
3. Federal PLUS Loan (Parent Loan for Undergraduate Students)
4. Private Education Loans
5. College Loans
6. State Loans

In addition to the above education loans, the family may want to look into the following loans to finance college:

1. Home Equity Loan
2. Life Insurance Loan
3. Business Loan
4. Intra Family Loan
5. Margin Account Loan
6. Credit Card Loan
7. Retirement Plan Loan

## **FEDERAL LOAN PROGRAM**

As of July 1, 2010, there will only be one program students and families can use to borrow federal student loans. That program is the William D. Ford Direct Loan Program (Direct Loan). Under this program the U.S. Department of Education will lend the funds to the student and parents.

### **FEDERAL SUBSIDIZED STAFFORD LOAN:**

The Federal Subsidized Stafford Loan is in the student's name and is the responsibility of the student. The Subsidized Stafford Loan is a need-based loan in which the Federal Government pays the interest on the loan until six months after the student leaves college. Loans disbursed before July 1, 2006, have a variable interest rate and are adjusted once a year on July 1<sup>st</sup>. The interest rate is capped at 8.25%. The interest rate on these loans for the 2010-2011 academic year is 2.47% for a student out of school. For loans disbursed between July 1, 2006 and June 30, 2008, the interest rate is fixed at 6.8%. For loans disbursed after July 1, 2010, the interest rate is fixed at 4.5% for undergraduate students and 6.8% for graduate students. There is a 1% insurance premium fee that is deducted from the loan proceeds. Payments on this loan start six months after the student has left school and can be deferred if the student goes back to school or in certain hardship cases. Interest paid by the student on these loans will qualify for the Student Loan Interest Deduction if the student's income is within the **\*Modified Adjusted Gross Income** limits of the IRS. This loan will qualify for consolidation under the Federal Loan Consolidation Program.

**\* Modified Adjusted Gross Income** (MAGI) for the Student Loan Interest Deduction for 2009 is: on Form 1040 it is found by taking line 38 and adding back line 33 (student loan interest deduction), line 34 (tuition and fees deduction), line 35 (domestic production activities deduction) and adding foreign earned income and housing exclusions, and/or foreign housing deduction; on Form 1040 A it is found by taking line 22 and adding line 18 (student loan interest deduction) and line 19 (tuition and fees deduction). For the 2009 tax year the Student

Loan Interest Deduction starts to phase out for married taxpayers filing jointly when their Modified Adjusted Gross Income reaches \$120,000 and goes completely away at \$150,000. For single or head of household taxpayers those limits are \$60,000 to \$75,000.

The amounts the student can borrow vary for each year of school and are as follows:

<u>Undergraduate Student</u>	<u>Dependent Student</u>
1 <sup>st</sup> year	\$ 3,500
2 <sup>nd</sup> year	\$ 4,500
3 <sup>rd</sup> and 4 <sup>th</sup> year	\$ 5,500 per year
5 <sup>th</sup> year if needed	\$ 4,000
<u>Graduate Student</u>	<u>Independent Student</u>
All Levels	\$ 8,500

**IMPORTANT** - On September 27, 2007, “College Cost Reduction and Access Act” was signed into law. One of the things this law did was to change the interest rates on Subsidized Stafford Loans. Effective October 1, 2007, interest rates on these loans have been reduced as follows:

- Loans disbursed after July 1, 2006 and before July 1, 2008 will have a fixed interest rate of 6.8%
- Loans disbursed after July 1, 2008 and before July 1, 2009 will have a fixed interest rate of 6%
- Loans disbursed after July 1, 2009 and before July 1, 2010 will have a fixed interest rate of 5.6%
- Loans disbursed after July 1, 2010 and before July 1, 2011 will have a fixed interest rate of 4.5%
- Loans disbursed after July 1, 2011 and before July 1, 2012 will have a fixed interest rate of 3.4%

On May 7, 2008, the “Ensuring Continued Access to Student Loans Act of 2008” was signed by the President. This law has a direct impact on the amount of Stafford Loans a student can take. For loans disbursed after July 1, 2008, a student may receive an additional \$2,000 Unsubsidized Stafford Loan for each of his four years in college in addition to his Subsidized Stafford Loan.

**NOTE:** The total undergraduate Stafford Loans (subsidized and unsubsidized) cannot exceed \$31,000 for a dependent student or \$57,500 for an independent student. The total graduate and undergraduate Stafford Loans (subsidized and unsubsidized) cannot exceed \$138,500.

**FEDERAL UNSUBSIDIZED STAFFORD LOAN:**

The Federal Unsubsidized Stafford Loan is in the student's name and is the responsibility of the student. The Unsubsidized Stafford Loan is not a need-based loan and interest starts to accrue on the loan immediately. If requested, the lender will waive interest payments while the student is in school and add this interest to the principal of the loan (Interest Capitalization). Loans disbursed before July 1, 2006, have a variable interest rate which is adjusted once a year on July 1<sup>st</sup>. The interest rate on this loan is capped at 8.25%. The present interest rate for 2010-2011 is 1.87% while the student is in college and 2.47% for a student out of school. For loans disbursed after July 1, 2006, the interest rate is fixed at 6.8% for both undergraduate and graduate students. There is a 1% insurance premium fee that is deducted from the loan proceeds. Payments on this loan start six months after the student has left school and can be deferred for students going back to school or in certain hardship cases. Interest paid by the student on these loans will qualify for the Student Loan Interest Deduction if the student's income is within the Modified Adjusted Gross Income Limits of the IRS. This loan will qualify for consolidation under the Federal Loan Consolidation Program.

The amounts the student can borrow vary for each year of school and after July 1, 2008 are as follows:

<u>Undergraduate Student</u>	<u>Dependent Student</u>	<u>Possible Additional Student Loan*</u>
1 <sup>st</sup> year	\$ 5,500	\$ 4,000
2 <sup>nd</sup> year	\$ 6,500	\$ 4,000
3 <sup>rd</sup> and 4 <sup>th</sup> year	\$ 7,500 per year	\$ 5,000 per year
5 <sup>th</sup> year	\$ 4,000	\$ 5,000
<u>Graduate Student</u>	<u>Independent Student</u>	
All levels	\$ 12,000 per year	

\* If you are an independent undergraduate student or a dependent student whose parents are unable to get a PLUS Loan, you may be eligible for these additional student loans. These loans are in addition to any Federal Subsidized or Unsubsidized Stafford Loan amounts received and are unsubsidized.

**NOTE:** The total undergraduate Stafford Loans (subsidized and unsubsidized) cannot exceed \$31,000 for a dependent student or \$57,500 for an independent student. The total graduate and undergraduate Stafford Loans (subsidized and unsubsidized) cannot exceed \$138,500.

**FEDERAL PERKINS LOAN:**

A Federal Perkins Loan is made by the school with funds from the Federal Capital Contributions (FCC), the school itself and collections from prior year Perkins Loans. The program is administered by the U.S. Department of Education and about 1,800 institutions participate.

The loan is in the student's name and is the responsibility of the student. This is a need-based loan in which the Federal Government pays the interest on the loan until nine months after the student leaves college. The interest rate is fixed at 5%. Payments on this loan start nine months after the student has left school and payments can be deferred for students going back to school or in certain hardship cases. The amount of the loan is determined by the college and can range up to \$5,500 per year for undergraduate students and up to \$8,000 for graduate students. The total undergraduate Perkins Loans can not exceed \$27,500. The total graduate and undergraduate Perkins Loans cannot exceed \$60,000. Interest paid by the student on these loans will qualify for the Student Loan Interest Deduction if the student's income is within the Modified Adjusted Gross Income Limits. This loan will also qualify for consolidation under the Federal Loan Consolidation Program. The Perkins Loan may be eligible for forgiveness under the "Federal Loan Cancellation" program.

**FEDERAL GRAD PLUS LOAN:**

This loan was established under the "Deficit Reduction Act of 2005" and is available to graduate students for academic years starting after July 1, 2006. This Federal Grad PLUS Loan is in the student's name. The loan is neither need-based nor merit-based. The student can borrow up to the total cost of college less any financial aid, other loans and/or distributions from certain educational tax benefit accounts. Loans first disbursed after June 30, 2010, have a fixed rate of 7.9%. Loans first disbursed prior to July 1, 2010, have a fixed rate of 7.9% if under the Direct Loan Program and 8.5% if under the FFEL Program. Payments on this loan start after the student has left school and are based on a ten year term. There is a 3% origination fee and a 1% insurance premium fee that are deducted from the loan proceeds. After the loan is disbursed, if the student dies or becomes totally disabled, the loan is forgiven. Interest paid by the student on this loan will qualify for the Student Loan Interest Deduction if the student's income is within the Modified Adjusted Gross Income Limits of the IRS. This loan will qualify for consolidation under the Federal Loan Consolidation Program.

**FEDERAL PARENT LOAN FOR UNDERGRADUATE STUDENTS (PLUS):**

The Federal PLUS Loan is in one of the parent's name. If one parent does not qualify for the loan the other parent can apply for the loan. This loan is neither need-based nor merit-based. Loans disbursed before July 1, 2006, have a

variable interest rate and are tied to the 91 Day Treasury Bill Rate as of May 31st of each year. The rate is adjusted once a year on July 1st and is capped at 9%. The interest rate for 2010-2011 is 3.27%. Loans disbursed after June 30, 2006, have a fixed interest rate. If the loan is under the Federal Direct Loan Program, the fixed interest rate is 7.9%. If the loan is under the Federal Family Education Loan Program (FFEL), the fixed interest rate is 8.5%. For all loans first disbursed after June 30, 2010, the interest rate is 7.9%. The term of the loan is 10 years. The amount that can be borrowed is the total cost of college less any financial aid and distributions from certain educational tax benefit accounts. If at any time the borrower dies or becomes totally disabled, the loan is forgiven. If the student for whom the PLUS Loan was taken dies, the loan is forgiven. There is a 3% origination fee and a 1% insurance premium fee that are deducted from the loan proceeds. Payments start within 60 days of the final disbursement of the loan.

As a result of the “Ensuring Continued Access to Student Loans Act of 2008” signed into law on May 7, 2008, the borrower has two options when repaying this loan. Those options are:

1. The borrower can make interest only payments while the student is in school and start payments of principal and interest after the student leaves school; or
2. The borrower can defer all payments until six months after the student leaves school. In this option the interest accrues and is added on to the loan when repayment begins.

Interest paid by the parent on this loan will qualify for the Student Loan Interest Deduction if the parents’ income is within the Modified Adjusted Gross Income Limits of the IRS. This loan will qualify for consolidation under the Federal Loan Consolidation Program.

**NOTE:** If both of the parents fail to qualify for a PLUS Loan, the student may qualify for an additional \$4,000/\$5,000 Stafford Loan.

## **PRIVATE EDUCATION LOAN**

The Private Education Loan is offered by a financial institution and is in the student’s name. Loans in the student’s name will almost always require a co-borrower. These loans are neither need-based nor merit based; they are credit based loans. The interest rate on these loans is variable with no cap on the rate. The rate can be based on the prime rate or the LIBOR Index plus a percentage and may be adjusted monthly or quarterly. Loans in the student’s name start repayment after the student has left school. The loan amount can be up to the total cost of college less any financial aid or a fixed annual dollar amount, which ever is lower. These loans are subject to various fees that are deducted from the loan proceeds. Interest paid on these loans will qualify for the Student Loan

Interest Deduction if the taxpayer/borrower's income is within the Modified Adjusted Gross Income Limits of the Internal Revenue Code.

As a result of the credit crisis of the past two years, these loans are hard to qualify for. The borrower (co-signer) has to have strong credit in order to qualify for these loans.

## **COLLEGE LOAN**

College loans administered by the college may come from the school's endowment or from a loan program set up with a financial institution. The loan is usually in the student's name. The interest rate could be variable or fixed and repayment usually begins after the student leaves school. The amount of the loan is determined by the college. Interest paid by the taxpayer/borrower on this loan will qualify for the Student Loan Interest Deduction if his income is within the Modified Adjusted Gross Income Limits of the Internal Revenue Code.

## **STATE LOAN**

Some states offer college loans to the student and/or parent. If these loans are available, it is best to check with the college to see what terms and conditions apply. Interest paid by the taxpayer/borrower will qualify for the Student Loan Interest Deduction if his income is within the Modified Adjusted Gross Income Limits of the Internal Revenue Code.

## **CONSOLIDATION OF EDUCATION LOANS**

There are two types of college loans that can be consolidated: federal loans that can be consolidated under the Federal Loan Consolidation Program and private education loans that can be consolidated with private lenders.

### **FEDERAL LOAN CONSOLIDATION PROGRAM:**

Under this program the borrower can consolidate the following federal loans:

1. Subsidized Stafford Loans
2. Unsubsidized Stafford Loans
3. Perkins Loans
4. PLUS Loans
5. Grad PLUS Loans

The borrower can only consolidate loans that are in his name: example - a Stafford Loan (student loan) cannot be consolidated with a PLUS Loan (parent loan).

The term of the loan is determined by the amount being consolidated and could be as long as 30 years. The interest rate is fixed and is the weighted average of the rates being consolidated. The rate is capped at 8.25%. The consolidation does not require an income or credit check of the borrower and can only be done after the student has left school. If the borrower goes back to school, the loan can go into deferment and if new education loans are incurred, they could be consolidated by themselves or with the first consolidation after the borrower leaves school. Federal student loans are consolidated with the U.S. Department of Education under the Direct Loan Program.

**NOTE:** Students and parents with federal loans disbursed before July 1, 2006, will want to wait until after June 30, 2010 because their variable rate loans will decrease slightly for 2010-2011.

**NOTE:** The "Health Care and Education Affordability Reconciliation Act of 2010" allows borrowers to consolidate federal student loans while "in-school" if they have at least one loan in two of the following three categories:

- Direct Loan Program
- FFEL Program
- Loans purchased by the U.S. Department of Education under ECASLA ("Ensuring Continued Access to Student Loans Act of 2008")

This "in-school" consolidation can only be done between July 1, 2010 and June 30, 2011 and if the borrower has not entered repayment on at least one of those loans.

### **PRIVATE LOAN CONSOLIDATIONS:**

Very few private lenders are consolidating private education loans. Those that do will base the loan on the credit worthiness of the borrower and may require a co-signer for the loan. Interest rates will be variable and usually tied to the prime rate or LIBOR Index plus a percentage, adjusted quarterly. The term of the loan will depend on the total amount of the loan and could be as long as 30 years. In some situations, fees may be associated with the loan.

## **FINAL NOTE**

The “College Cost Reduction and Access Act of 2007” included a section called “Income-Based Repayment” (IBR). Starting July 1, 2009, students who are in repayment or about to start payments on their federal student loans should see if they qualify for IBR.

If the student qualifies, the monthly loan payment is based on annual income and not the amount of the loan. This is a complicated area, so if you think you may qualify for IBR, contact a professional who can help you through the process.

## **WEB SITES – EDUCATION LOANS**

<b><u>Lender</u></b>	<b><u>Web Site</u></b>
Citibank	<a href="http://www.studentloan.com">www.studentloan.com</a>
Chase	<a href="http://www.chase.com">www.chase.com</a>
Key Bank	<a href="http://www.key.com/educate">www.key.com/educate</a>
PNC Bank	<a href="http://www.eduloans.pncbank.com">www.eduloans.pncbank.com</a>
Citizen's Bank	<a href="http://www.citizensbank.com">www.citizensbank.com</a>
US Bank	<a href="http://www.usbank.com">www.usbank.com</a>
Wells Fargo	<a href="http://www.wellsfargo.com">www.wellsfargo.com</a>
William D. Ford Direct Loan Program (for Consolidation Loans)	<a href="http://www.dl.ed.gov">www.dl.ed.gov</a> <a href="http://www.loanconsolidation.ed.gov">www.loanconsolidation.ed.gov</a>
National Student Loan Data System	<a href="http://www.nslds.ed.gov">www.nslds.ed.gov</a>

We do not recommend one lender over another when providing this list. There are additional lenders that you may want to consider when applying for an educational loan.