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Guide to Dealing with Student Loan Debt

Depending on your financial situation and the status of your loans, there are different strategies for dealing with student loan debt. This handout is intended to help as a guide to addressing payment options and relief strategies for consumers struggling with their student loans.

Private or Federal Student Loans?

The first step to dealing with student loan debt is to identify what type of loan you have: federal or private. The federal government has set up a website that gives a complete history of federal student loans.

To determine the type of your loan: www.nslds.ed.gov

If your loan is not listed on your individual report, it is very likely a private student loan. If your loan is listed, you know that it is a federal student loan. The report will also identify the type of federal loan you have (Stafford, Perkins, Graduate Plus, etc.), and the status of those loans (good standing, default, delinquent).

Federal Student Loans

No payment is due on federal student loans while you are enrolled in school. Usually, there is a 6 month grace period for Stafford and Graduate Plus loans, and a 9 month grace period for Perkins loans where no payment is required. After the grace period ends, you enter repayment.

**If you do not select a payment plan upon entering repayment, the default monthly payment plan is based on a 10 year payback schedule, which does not function well for low income student loan borrowers.

Deferment and Forbearance – Federal Student Loans

Federal loans are classified as subsidized or unsubsidized on your NSLDS report. Under deferment, your loan payments are postponed and no interest accrues on subsidized loans. Under forbearance, your loan payments are postponed but interest continues to accrue.

You must apply to your loan servicer to receive a deferment or forbearance: https://studentaid.ed.gov/sa/repay-loans/deferment-forbearance

Repayment Options – Federal Student Loans

Repayment options for federal student loans are dependent on the type of federal loan you have. Prior to July 2010, federal student loans were issued through the Federal Family Education Loan Program ("FFEL"). After July 2010, federal student loans were issued through the William D. Ford Federal Direct Loan Program ("Direct"). The main difference is that the originator for Direct loans is the Department of Education instead of a bank insured by a Guarantor in the FFEL program. Your "NSLDS" report referenced above will indicate what loan program you have.

Repayment Calculator

The Department of Education has a VERY HELPFUL online repayment calculator which helps estimate monthly payment options for federal loan borrowers:
https://studentloans.gov/myDirectLoan/mobile/repayment/repaymentEstimator.action

Loans in the FFEL program can be "consolidated" (refinanced) into a direct loan and become eligible for payback options as well. Federal consolidation loans are not based on credit, and will generally be approved.
https://studentloans.gov/myDirectLoan/whatYouNeed.action?page=loanConsol

Here's a summary of the most common payback options provided by the calculator:

Qualifying Payment Payback Options: Payments under most plans are "qualifying payments" as defined by the Department of Education (each payment counts toward loan forgiveness programs). Non-qualifying payback options through the Direct Loan Program include the Graduated, Extended, and Extended Graduated Programs. Payments through non-qualified programs might offer the lowest monthly payment for borrowers, but again, these payments do not count toward debt forgiveness programs. See below for more information on these programs.

****10 year standard repayment**: This is the default payback option if no plan is selected after you enter repayment for a federal loan. The loan's principal and interest is paid off in its entirety, on a 10 year payback schedule.

Income Driven Repayment Options: Income driven plans are based off of household size and income: https://studentaid.ed.gov/sa/repay-loans/understand/plans/income-driven

****REPAYE:** New Program as of December 2015. Gives all Direct loan student borrowers the ability to cap their monthly payments at 10% of their "discretionary income," defined as adjusted gross income above 150% of the applicable poverty guideline divided by twelve.

- ** Entire balance of student loan forgiven after 25 years of payments
- ** Monthly payment amount based on 10% of disposable income which is based on household size
- ** Student must re-certify income annually
- ** Discharged amount may be taxable with a 1099 being issued
- ** Parent Plus loans are not eligible
- ** If borrower is married, both spouses' income used for calculation

Example: Borrower is mother of two children with adjusted gross income of $20,000 annually. Her disposable income is $0. 10% of disposable income results in a $0/payment. If her income never goes up, she will never have a student loan payment. After 25 years, the entire balance of her loan will be forgiven.

****Income Contingent Repayment:** Income Contingent Repayment ("ICR") is based on 20% of disposable income and features forgiveness after 25 years. Importantly, Parent Plus loans which are consolidated into the Direct Loan Program are eligible for ICR.

****Income Based Repayment**: A borrower qualifies for Income Based Repayment ("IBR") if IBR payment is less than 10 year standard. Perkins loans must be consolidated in order to be eligible. Parent Plus loans cannot have IBR, even if consolidated. However, household income in IBR, if taxpayers file separately, is calculated only on the student borrower's income. If a joint tax return is filed, both spouses' income is used in the calculation.

Non-qualifying payments: Graduated, Extended Fixed, and Extended Graduated are all payback programs for federal student loans where each monthly payment does not count toward forgiveness programs outlined below.

Forgiveness

Administrative Discharge – Federal Student Loans

A finding of "Total and Permanent Disability ("TPD")" by the federal government will result in an administrative discharge of federal student loan obligations. Usually, a finding of permanent disability by the Social Security Administration with a 5 to 7 year review period will qualify a student for this type of relief. Documentation of a medical condition from doctors or the Veterans Administration will also be considered by the Department of Education.

How to apply for TPD from the Department of Education: https://studentaid.ed.gov/sa/repay-loans/forgiveness-cancellation/disability-discharge

**Death of the student discharges Parent Plus loans
**Closed School: Borrower must have been enrolled or withdrawn within 90 days of closure

Public Service Forgiveness: Tax free discharge with 120 "qualifying payments," in as short as 10 years.

** Must work for a qualifying employer: 501(c)(3) or government (ie Mission Hospital, UNC-Asheville, AB Tech, or Habitat for Humanity)
** Work must be full-time, 30 or more hours a week
** Qualifying payments include REPAYE program based on 10% of disposable income (and other Income-Driven Plans)

Teacher Loan Forgiveness: $17,500 of forgiveness for full time, 5 consecutive years

** Math, science in eligible secondary school
** Special education in secondary or elementary school
** $5,000 of forgiveness for other teachers with same criteria
** Not available if loan balance existed prior to 1998

**To qualify for public service forgiveness programs, you must select a repayment option which counts toward forgiveness as a "qualifying payment" as referenced above.

Dealing with Default

After federal student loan borrowers miss payments, they are "delinquent" for the first 270 days. After 270 days, their loan goes into "default."

**Collection Fee: Collectors can charge up to 25% of the student loan principal after default occurs

**Wage Garnishment: Capped at 15% of disposable pay; notice sent 30 days prior to start of garnishment

**Tax Refund Intercept: Federal government can withhold any tax refunds due to borrower; injured spouse form may be filed by borrower's spouse in order to keep the non-borrowering spouse's portion of the refund

**Social Security Offset: Capped at 15%

**Lawsuit: Usually only used when no attachable wages exist; minimum $10,000 balance for Department of Justice to file suit; less common than other collection methods

**Ineligible for Federal employment

Curing Default

There are two common ways to cure a default on a federal student loan: consolidation and rehabilitation.

Consolidation: A borrower can cure default by consolidating their defaulted loans into the Direct Loan program. This type of "refinance" transaction cures the default by paying off the old loans. The new loans are eligible for the payback options discussed above. The process can be done online, takes about 60-90 days, and may require a debtor to pay an 18.5% "cure" fee.

    ** Not eligible for consolidation after a wage garnishment has begun

Rehabilitation: A borrower can cure default by rehabilitating their defaulted loans. Rehabilitation is defined as making 9 payments within a 10 month period, and may require the same 18.5% "cure" fee. The required monthly payment must be "reasonable and affordable," and many times is based on the required payment in the REPAYE program.

    ** Can only rehabilitate a defaulted loan once
    ** Default notation is removed from a borrower's credit report
    ** 5th payment ceases wage garnishments

Private Student Loans

Private student lenders are not required to provide borrowers with the payback options in the Direct Loan program discussed above. However, private student lenders are restricted on how they can collect by state law. In North Carolina, that means no wage garnishment. The private lender would need to achieve a state court judgment, serve exemption notices, and then collect only against non-exempt property belonging to the borrower.

A few more differences:

- ** No grace period: Repayment usually begins immediately when school ends
- ** Repayment: Some lenders offer forbearances or interest-only payments for 2 to 3 years; no direct loan payback options

Lawsuit Defense: Defending a private student loan lawsuit can be similar to defending any other type of collection lawsuit from a debt collector.

- ** Statute of limitations: Typically 3 years for North Carolina resident
- ** Chain of title: Plaintiff must prove ownership of debt

Dealing with Student Loans through Bankruptcy

Private student loans which are uncollectible under North Carolina law can be discharged in a Chapter 7 or Chapter 13 bankruptcy case.

Federal loans are restricted from discharge unless a debtor can prove "undue hardship" under the Brunner test. While the law may be changing, it is usually more simple and efficient to apply for an administrative discharge discussed above rather than to file the required adversary proceeding in Chapter 7 or 13 bankruptcy seeking a discharge.

In Chapter 13, federal student loans are placed on an administrative forbearance, so no payment is required, and interest continues to accrue on a debtor's student loans. Borrowers in Chapter 13 may choose to continue private student loan payments outside of their Chapter 13 payments to decrease their student loan balances accordingly, but no payment is required outside of Chapter 13.

Recently, for the first time in North Carolina, a debtor's proposed Chapter 13 plan was confirmed with a provision for an Income-Driven Plan Payment. For debtor's with large balances, this would make a huge difference in the effectiveness of their "fresh start" promised by the Bankruptcy Code.