**Loan Repayment:**

**A Primer for Surgeons**

***Financial Literacy Lecture Series***

***Resident and Associate Society—American College of Surgeons (RAS-ACS)***

***Education Committee***

***Contributors:***

Elissa Falconer, MD

Kaitlin A. Ritter, MD

***“When you run in debt, you give to another power over your liberty.”***

– Benjamin Franklin

With the rising cost of undergraduate and graduate education, students are increasingly relying upon student loans in order to finance their education. As of 2020, about 30% of Americans reported having student debt with the average public university student borrowing ~$30,000 to attain a bachelor’s degree. With this mounting issue of education debt, it is critical for borrowers to understand the basics of student loans both federal and private. By educating themselves about the basic of loan administration, types, and repayment, students can equip themselves with the knowledge to achieve their educational goals with a thoughtful and financially sound economic plan.

This resource aims to provider readers with a general overview of student loan programs, interest, and repayment strategies. We herein focus largely on federal student loans, but the overview of loan terminology can be useful for understanding both federal and private loans.

***Note: This content is for informational purpose only and should not be taken as official financial advice. All borrowers should perform their own research prior to engaging in any financial transactions.***

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1. **COMMON LOAN TYPES-PROS/CONS**
2. Federal Loans- loans from the federal government to be used to pay for undergraduate/graduate education

*Pros:* Loan terms and conditions are set by law and often have better benefits (i.e. fixed interest rates, income based repayment options and public service loan forgiveness) as compared to private loans which are regulated by the individual loan provider/bank

*Cons:* Federal student loans do not qualify for bankruptcy, meaning you will still have to pay these loans back even if you declare bankruptcy. There are no subsidized federal loan options for graduate students. Subsidized loans are only available for undergraduate education.

* 1. Direct Student Loan Types
		1. **Direct/Stafford Subsidized Loans**- these loans are made available to undergraduate students only and loan amounts are based upon financial need. The loan is subsidized which means the loan interest is paid by the U.S. Department of Education while you are in school (at least half-time), during your grace period (the first six months after you leave school) and during periods of forbearance.
		2. **Direct/Stafford Unsubsidized Loans** – these loans are made available to undergraduate ***and*** graduate students. This type of loan has no financial need requirement. Unsubsidized means that the borrower must cover the cost of interest including while you are in school and during grace/deferment periods. If you choose not make interest payments while in school, the interest is added to your total loan amount.
		3. **Direct PLUS Loans**—these loans are made available to graduate or professional students only. They require a credit check and are available only to borrowers without an adverse credit history. They have the benefit of a fixed interest rate, income driven repayment, and loan forgiveness, but are unsubsidized and interest accrues during school and is added to your total loan amount. While the interest rate is fixed, this loan type has the highest interest rate of all the direct loans. These loans can be made directly to the student (Grad PLUS) or to the parents of a student (Parent PLUS). Limitations exist in repayment options.
		4. **Direct Consolidation Loans**—these loans allow you to combine several of your federal loans into a single loan allowing you to make one monthly payment instead of several payments for several loans. You are able to combine different types of loans including direct, indirect/FFEL, and Plus loans. There are certain limitations in regard to repayment options.
	2. Indirect Student Loans

Also known as the Federal Family Education Loan Program (FFEL), these loans were funded by private lenders (i.e. banks, credit unions), but were guaranteed by the federal government. They were created to encourage private lenders to loan money to borrowers such as students who have little to no credit and have a financial need. By having the federal government guarantee the loan, these loans were of little risk to the lenders. This program was ended in 2010 since the Direct Loan Program largely replaced the need for indirect loans. These loans have the benefit of income-based repayment, but do not qualify for public service loan forgiveness.

* 1. Perkins Loans

This loan program was designed for undergraduate and graduate borrowers who had exceptional financial need (above that of a traditional direct loan). They were subsidized loans with a low interest rate, a nine-month grace period before repayment was required and qualify for loan forgiveness. This program was terminated in 2018 due to budget concerns.

1. Private Loans- loans from private institutions such as banks, credit unions, and student loan agencies

*Pros*: Private lenders have more flexibility in interest rates and can offer lower rates for borrowers with good credit, often offer higher borrowing limits and can help cover the difference between school costs and federal loan limits, in some situations private student loans can qualify for bankruptcy if necessary

*Cons:* loans do not qualify for income-based repayment or public service loan forgiveness, can have variable interest rates versus the fixed rates of federal loans, often require a co-signer

1. Health Professions Student Loans- loans administered through the Health Resources and Services Administration (HRSA) that are made available for students pursuing heath profession degrees including doctorates, nursing degrees and primary care physician.

*Pros*: these are low fixed interest rate loans which are subsidized during school and grace periods, have a 9-12 month grace period depending on exact program type, offer a deferment period for residency/fellowship, active duty service, and leaves of absence for related educational activities such as joint degree programs during which interest does not accrue.

*Cons*: required to work in an underserved area or within a particular field (such as primary care) until the loan is repaid, must be a U.S. citizen or permanent resident, loan amounts are limited and based upon the school’s cost of attendance

Loan Programs

1. Health Professions Student Loans (HPSL)- for students pursuing degrees in dentistry, optometry, veterinary medicine, podiatry or pharmacy
2. Nursing Student Loans/Nursing School Loans (NSL)- for student’s pursing associate, bachelor’s or master’s degrees in nursing
3. HRSA Primary Care Loans (PCL)- for students pursing doctoral degrees in allopathic medicine or osteopathic medicine
4. Loans for Disadvantaged Students (LDS)- for students from disadvantaged backgrounds pursing doctoral degrees in any of the above areas, excludes nursing degrees
5. **UNDERSTANDING INTEREST**

What is interest?

Interest is the amount that a lender charges borrowers for lending them money. It is usually expressed as an annual percentage rate (APR) or in layman’s terms the “interest rate.” Interest rates can vary depending upon the loan type, borrower credit history, length of loan, inflation rates and other factors.

What different types of interest rates are there?

Interest can be applied to a loan in a variety of different ways. The two primary types of interest rates are fixed and variable.

1. Fixed interest rates- loans with fixed interest rates have the same interest rates for the entirety of the borrowing period
2. Variable interest rates-loans with variable interest rates will have changes in their interest rates over the course of the borrowing period. This can benefit borrowers if there are improvements in the market/economy with lowering rates. In times of recession and financial instability, interest rates often go up.

 Interest can be calculated in two different ways—simple and compound.

1. Simple interest- interest is calculated based off of the principal amount/the amount initially borrowed. If you borrow $10,000 at a 2% annual interest rate you will be charged $200 in interest and that will be added to your loan amount. Next year, even though your loan is now $10,200, your interest will only be calculated on the initially $10,000.
2. Compound interest- interest is calculated off the initial amount borrowed and any interest that has accrued in previous years. In our $10,000 example, at the end of year 1 your new loan total is $10,200. Interest for year 2 will be calculated based on the total $10,200. This amounts to paying interest on your interest. Interest can be compounded at variable rates meaning your accumulated interest can be added to the principle at different time points. While the frequency of compounding varies with each loan compounding can occur daily, weekly, monthly or yearly. The more frequently your interest is compounded, the higher your end total loan cost will be.

What is capitalization?

Capitalization refers to the process of adding your accrued unpaid interest to your principle loan amount. If you borrow $10,000 dollars at 2% interest and pay your annual $200 when the loan is capitalized at the time of graduation, no extra money will be added. If, however, you do not pay off the accrued interest and have $1000 dollars in interest accrued, this will be added to your base loan of $10,000 making your new loan $11,000. This $11,000 is what you will be charged interest on going forward. Capitalization is similar to compounding interest, but does not occur on a regular basis. Instead, loans capitalize at certain pre-specific times such as the end of the grace period, after a period of deferment/forbearance or when you change your income-based repayment plan.

What are subsidized and unsubsidized loans?

Subsidized loan simply means that during a designated period, the interest on the loan is paid by a second party. In the case of many federal student loans, the interest is paid by the U.S. Department of Education while a borrower is still in school, within the grace period, or approved deferment periods. In unsubsidized loans, the interest is not paid during these periods (unless you elect to pay it personally) and it added to total principle amount at the time of capitalization.

1. **CONSOLIDATION AND REFINANCING**

Consolidation is the act of taking out a new loan to pay off other loans and debts. By doing this, the borrower takes all of their loans with often varying interest rates and repayment plans and simplifies all the debt into one loan. Loan consolidation often allows for a single interest rate for all your loans, making a single monthly payment, and makes general loan management easier for the borrower.

Borrowers with federal student loans have the option to consolidate their loans with the U.S. Department of Education through the Direct Consolidation Loan Program. This can be of benefit to borrowers with variable interest rate loans or Perkins/Indirect loans which do not qualify for PSLF. (Consolidating Perkins/Indirect loans can make these loan payments qualify for PSLF under certain repayment plans). Importantly with the Direct Consolidation Loan Program, at the time of consolidation any accrued interest capitalizes and is added to the loan principle. *You also lose credit for any qualifying payments you may have made to PSLF. This is extremely important, especially if you have made a significant portion of qualifying payments, as consolidation resets your PSLF payments back to zero.* The exact terms of consolidation are available on the federal student loan website and should be carefully reviewed before any changes are performed.

Refinancing is the same as consolidation, but refers to the combining of private and federal loans by a private institution such as a bank. While consolidation only allows you to combine your federal loans, many borrowers have both private and federal loans to help cover the total cost of their education. Refinancing can combine all of your private loans or your private and federal loans. Importantly, if you refinance and include your federal loans, you lose the federal loan protection benefits including income based repayment and your loan payments no longer qualify for PSLF.

1. **REPAYMENT OPTIONS**

Loan repayment options vary with the type of loan and the loan servicer (federal v. private loans). Below describes the repayment options for federal student loans, but private lenders may have similar options available

1. Standard Repayment Plan\*- monthly payments are fixed amounts that make sure you pay off your loans within the loan period (typically 10 years)
2. Graduated Repayment Plan\*- monthly payments are lower at first and then increase every two years to ensure loans are paid off within the loan period, good for borrowers who have low initial incomes, but higher eventual earning potential
3. Extended Repayment Plan\*- monthly payments which can be fixed or graduated which are paid out over 25 years, you pay more in interest, but your monthly payments will be lower. Must have > $30,000 in outstanding loans to qualify
4. Revised Pay As You Earn Repayment Plan (REPAYE)- monthly payments are 10% of your discretionary income, payment amount re-calculated each year based upon your updated income and family size, includes your spouse’s income and loan debt in monthly payment calculations, outstanding loans forgiven after 20/25 years, for direct loans only
5. Pay As You Earn Repayment Plan (PAYE)- monthly payments are 10% of your discretionary income, payment amount re-calculated each year based upon your updated income and family size, spouse’s income only included if you file income taxes jointly, may need to consolidate loans to qualify, outstanding loan forgiveness after 20 years, for direct loans only
6. Income-Based Repayment Plan (IBR)- monthly payments 10-15% of discretionary income (depending upon when loans were taken out), payment amount re-calculated each year based upon your updated income and family size, spouse’s income only included if you file income taxes jointly, outstanding loans forgiven after 20/25 years, for direct loans only
7. Income-Contingent Repayment Plan (ICR)- monthly payments are 20% of discretionary income or the amount you would pay on a fixed payment 12 year plan (whichever is less), spouse’s income only included if you file income taxes jointly, parent borrowers can enroll in this plan if they consolidate their child’s loans
8. Income-Sensitive Repayment Plan\*- for Indirect student loans only, monthly payment based on annual income to make sure loan paid in full within 15 years

\*These repayment strategies do NOT qualify the borrower for Public Service Loan Forgiveness. If you are interested in pursuing PSLF you should not use these plans as your repayment strategy.

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| **Repayment Plan** | **Loan Type** | **Monthly Payment** | **Spousal Income** | **PSLF Qual.** | **Loan Forgiv.** | **Pros** | **Cons** |
| Standard | - Direct Sub and Unsub- Indirect Sub and Unsub- All PLUS loans- All consolidated loans | Fixed | n/a | No | No | -quickest pay off-least amount of interest paid-spousal income does not affect payments-pay off in 10 years | -no income adjustment -higher monthly payments |
| Graduated | - Direct Sub and Unsub- Indirect Sub and Unsub- All PLUS loans- All consolidated loans | Biennial increase | n/a | No | No | -graduated payment increases-lower total interest -spousal income does not affect payments-pay off in 10 years | -no income adjustment-higher monthly payments |
| Extended | - Direct Sub and Unsub- Indirect Sub and Unsub- All PLUS loans- All consolidated loans | Fixed or Graduated | n/a | No | No | -lower monthly payments then standard | -no income adjustment-pay off in 25 years |
| REPAYE | -Direct Sub and Unsub-Direct PLUS loans (students)-Direct consolid. loans without parent PLUS or indirect/FFEL loans | 10% discretionary income | Joint income always counted | Yes | Yes- 20 or 25 years | -qualifies PSLF-income based repayment | -Direct loans only-Direct PLUS parent loans don’t qualify-higher total interest payment |
| PAYE | -Direct Sub and Unsub-Direct PLUS loans (students)-Direct consolid. loans without parent PLUS or indirect/FFEL loans | 10% discretionary income | Joint income if filling jointlyIf single file, spouse not counted | Yes | Yes- 20 years | -qualifies PSLF- 10% monthly payment will never be more than standard repayment plan (caps out)-income based repayment | -Direct loans only-Direct PLUS parent loans don’t qualify-higher total interest payment |
| IBR | -Direct Sub and Unsub-Direct PLUS loans (students)-Direct consolid. loans without parent PLUS or indirect/FFEL loans | 10-15% discretionary income | Joint income if filling jointlyIf single file, spouse not counted | Yes | Yes- 20 or 25 years | -qualifies PSLF- income based repayment | -higher monthly payments then other income based plans-Direct loans only-Direct PLUS parent loans don’t qualify-higher total interest payment |
| ICR | -Direct Sub and Unsub-Direct PLUS loans (students)-All consolidated loans included indirect/FFEL and parent PLUS | 20% discretionary income orFixed payment over 12 years | Joint income if filling jointlyIf single file, spouse not counted | Yes | Yes- 25 years | -qualifies PSLF-parent PLUS loans included-two monthly calculations, pay the lesser amount | -higher total interest payments -payments can be above standard repayment plans |
| ISR | -Indirect/FFEL loans | Varies by lender | -- | No | No | -income based payments | -must pay off loan in 15 yrs which can result in high payments |

1. **PUBLIC SERVICE LOAN FORGIVENESS**

Public Service Loan Forgiveness (PSLF) is a federal loan forgiveness program that forgives the remaining balance on your student loans after you have made 120 qualifying monthly payments.

This program has requirements which include:

1. Be employed by a U.S. federal, state, local or tribal government or a not-for-profit organization (tax-exempt under Section 501(c)(3)), includes U.S. military service
2. Work full time for that organization- your employer’s definition of full time or at least 30 hrs per week, whichever is greater
3. Have Direct loans- Indirect/FFEL loans and Perkins loans do not qualify, but if consolidated into a direct loan may become eligible
4. Repay your loans under an income-drive repayment plan (REPAYE, PAYE, IBR, or ICR)
5. Make 120 qualifying payments- must make a full monthly payment that is no more than 15 days after your due date while employed full time by a qualifying employer

Employer certification

As part of the PSLF loan forgiveness you must work for a qualified employer. This is confirmed and documented by submission of an employment certification form. This form is filled out by you and your employer and then submitted to the U.S. Department of Education. The form is processed and the administering body of PSLF who confirms that your employer meets the program qualifications. Once you have completed your 120 qualifying payments you must submit the employment certification form for all of your qualifying employers to get credit for these payments. You can submit this form periodically throughout your repayment period preemptively confirming your employer qualifies and registering qualified payments with the PSLF program. It is recommend to submit these certifications regularly through your repayment period because it will allow you and the PSLF program to track your qualifying payments and avoid any surprises at the end of the repayment period.

Qualifying payments

Qualifying payments mean a full, on time payment (no later than 15 days late) paid during qualifying periods. Qualifying monthly payments do not occur during in-school status, grace period, and deferment/forbearance. Any payments made during these times will contribute to paying down your total loan cost, but will not count towards your required 120 payments. Multiple payments made during a single month will also not count towards your requirement payments. Only one full on time payment per month is counted. This means it will take a minimum of 10 years to meet your qualifying payments (assuming no missed payments).

Of note during the COVID19 pandemic the federal government placed on pause on loan repayment for borrowers. All eligible loans were placed on a 0% interest rate and a total monthly payment of $0. If you did not make payments during this loan freeze, each month still counted as a qualifying payment for PSLF.

1. **DEFERMENT/FORBEARANCE**

Deferment and forbearance are two ways in which borrowers can temporarily postpone of reduce their federal student loan payments.

In deferment, typically no interest accrues on your loans during this period. (This applies only to Direct/Stafford Subsidized and Federal Perkins loans. Direct Unsubsidized, Indirect/FFEL and Direct plus loans still accrue interest). Deferments are not automatic and borrowers must submit an application and meet certain requirements. Major eligibility groups include:

1. Cancer treatment deferment
2. Economic hardship deferment
3. Graduate fellowship deferment
4. In-school deferment (this deferment is automatic)
5. Military service/Post active-duty student deferment
6. Parent PLUS borrower deferment
7. Rehabilitation training deferment
8. Unemployment deferment

In forbearance, interest continue to accrue on your loans during this period of non-payment. At the end of your forbearance the unpaid accrued interest is capitalized and added to your loan principle. (If you continue to pay your interest in full during your forbearance no additional cost will be added). Forbearances are not automatic and borrowers must submit an application. There are two main types of forbearance- General and Mandatory.

General Forbearance- also known as discretionary forbearance, this type of forbearance is based upon a request of your loan servicer. They are not obligated to grant your forbearance. Usual reasons for forbearance include:

1. Financial difficulties
2. Medical expenses
3. Change in employment
4. Other reasons acceptable to your loan servicer

General forbearances are granted for no longer than 12 months at a time, but can be renewed at the end of your current forbearance. There is a maximum of three years of forbearance.

Mandatory Forbearance-in this type of forbearance as long as you meet certain eligibility requirements, the loan servicer is required to grant you forbearance. Common mandatory circumstances include:

1. Serving in an AmeriCorp position
2. Qualify for Department of Defense Student Loan Repayment Program
3. Medical or dental internship/residency
4. National guard duty
5. Student loan debt burden-monthly payment >20% of your monthly gross income
6. Teacher loan forgiveness

Mandatory forbearances are granted for no longer than 12 months at a time, but can be renewed at the end of your current forbearance. Some circumstances have limits on the length of forbearance.

1. **WHAT IF I DIE/BECOME DISABLED?**

While this is a morbid subject, death and disability can significantly impact a person and their family both emotionally and financially. In the event of the borrower’s death, federal student loans are discharged (forgiven) including loans taken out by a borrower’s parents (parent PLUS loans). If borrowers were to become seriously disabled such that you are unable to engage in substantial gainful activity due to a physical or mental impairment, they are able to apply for total and permanent disability discharge (TPD). TPD has several requirements including documentation of disability by a physician and annual earning limits. It requires a formal application which can be completed by the borrower or borrower’s family. It is possible for student loans to be re-instated after TPD if the borrower no longer meets requirements and the value of loan forgiveness may be taxable.