# Strategies for Managing College Debts

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The average law student incurs more than $140,000 in student loans, according to a 2017 survey. These debts can be a significant roadblock on the path to prosperity and retirement. Fortunately, there are strategies young attorneys can employ to reduce the impact of these debts on their financial futures.

The type of lender makes a big difference in repaying student loans. Private lenders want their money back ... period. Those without the ability to independently qualify for the loan may require a co-signer who will be required to ensure the loan is repaid. Many federal loans have more flexibility with programs designed to ease the burden.

Every borrower's first loan repayment option is to follow the standard repayment schedule. It is rigid but predictable. There is a set date when the loan will be satisfied ... 20-30 years after graduation. Other repayment options offer flexible payments and even debt forgiveness. Bear in mind that interest rates have been historically low for a decade. Future interest rates may be higher and more burdensome. Any strategy that extends the life of the loan may cost more in the long term.

## Income-Based Repayment (IBR/ICR)

Under a program available since 2009, borrowers may qualify for reduced payments and loan forgiveness based on their income. In income-based plans, borrowers with joint income below 15 percent of the poverty level for their family size may have lower monthly payments. Earning more will cap the loan payment at 15 percent of the earnings above the threshold. After 20-25 years of qualifying (depending on the program), the loan may be forgiven.

Because the payments are reduced, it is possible they may not cover added interest. This means that the future loan balance may be higher than the initial amount borrowed. That is a lot to pay back if the borrower ceases qualifying for income-based repayment.

## Pay As You Earn (PAYE)

Pay as you earn is a repayment option for federal student loans that has been available since 2012. This program is very similar to IBR (as far as income qualification levels) with loan forgiveness possible after 20 years of qualifying payments. Borrowers earning less than 150 percent of the poverty level based on family size may not even be required to make a payment. Earning more will cap the loan payment at 10 percent of the earnings above the threshold.

## Public Service Loan Forgiveness (PSLF)

Public Service Loan Forgiveness is a program for federal student loan borrowers employed primarily in public service. This program forgives remaining debt after 10 years of eligible employment and qualifying loan payments. During those 10 years, the income-based repayment programs can help to keep loan payments affordable. This program is for people with federal student loans who work in "public service," including jobs in government and nonprofit 501(c)(3) organizations. Other organizations may also be eligible if they are non-profit, non-religious, non-political and provide public services related to elder services, childhood education, or public safety.

Only payments made after Oct. 1, 2007, count toward the 10 years – and they do not have to be consecutive. To count, payments must be made while working full-time in eligible employment. Qualification may occur in retrospect with certification of employment and qualifying payments.

Federal Perkins Loans are unique. These loans may be forgiven after five years of eligible employment and qualifying payments. Attorneys with this type of loan should talk to their loan servicer to make sure they are taking full advantage of the benefits.

## A Note of Caution

Loan forgiveness is powerful and beneficial to building wealth. However, the program under which a student loan is forgiven has consequences. When loans are forgiven under the income-based options, the amount forgiven is imputed to the borrower as income – potentially generating a significant tax bill. If interest has been accumulating under reduced payment schedules, the amount forgiven could be higher than the original amount borrowed! Loans forgiven under PSLF do not generate income for the borrower.

## Debt Consolidation

Federal loans may be consolidated and still qualify for IBR/ICR and PSLF programs. Before any debt consolidation, ensure continued program eligibility before making the change. Each debt consolidation resets the repayment schedule and interest rates. Given the trade-offs between debt repayment and potential future imputed income, navigate these waters with care and guidance from loan servicers. Those with Perkins Loans should be careful to preserve their character in any debt consolidation.

## How Does This Help?

Lowering the payments on loans may help build wealth by freeing current income for retirement plan contributions and other investments. At some point, everyone will need money for an emergency or to fund retirement.

The above list is not exhaustive. There are additional loan programs available through States and private companies. To determine individual applicability, please consult a loan counselor.

Patrick Yanke is a Raleigh financial planner with a simple business philosophy: Treat others as he wants to be treated. He has a national business with clients in every American time zone. He delivers newsletters, and speaking programs on a wide range of financial topics. Opinions expressed here are Patrick Yanke's and not necessarily those of Raymond James. You should discuss any tax and legal matters with the appropriate professional. www.yankefinancial.com.