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Are Your Student Loans Forgivable?

July 9, 2020

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Student loan debt is a significant burden that can threaten to derail our financial goals. Fortunately, several options exist that can help make this type of debt more manageable. Retirement Director Ben Rizzuto discusses one option – loan forgiveness – and offers guidance on how to best navigate the process through the Public Service Loan Forgiveness (PSLF) program.

With student loan debt exceeding $1.5 trillion in the U.S., it has become essential for borrowers to understand their options for managing these burdens, which can represent a huge portion of an individual's budget. From payment plans to consolidation to loan forgiveness, there are a number of avenues to explore as part of the financial planning associated with debt management.

Depending on the career they have chosen, forgiveness is one option that may be available to many people struggling with student loan debt. In this post, we'll go over several things people need to understand regarding the Public Service Loan Forgiveness (PSLF) program.

Who Qualifies?

The Federal Student Aid website (www.studentaid.gov) is quite clear in its description of who qualifies for the PSLF program: "It isn't about the specific job that you do for your employer. Instead, it's about who your employer is." So, what types of employers qualify for loan forgiveness?

Qualifying employers include government organizations at any level (U.S. federal, state, local or tribal) and not-for-profit organizations that are tax exempt under Section 501(c)(3) of the Internal Revenue Code. Serving as a full-time AmeriCorps or Peace Corps volunteer also qualifies an individual for loan forgiveness, and employers that provide the following services are eligible as well:

- Military service
- Public safety
- Law enforcement
- Public interest legal services
- Early childhood education
- Public service for individuals with disabilities
- Public service for the elderly
- Public health
- Public education
- Public library services
- School library services

That's a fairly extensive list. But which types of employers do <u>not</u> qualify for PSLF? That list includes labor unions, partisan political organizations and for-profit organizations (including for-profit government contractors).

If you work for one of the types of employers that qualify, the best place to start the loan forgiveness process is by completing the Employer Certification Form (located on the studentaid.gov website).

What Types of Loans Qualify?

If you've verified that your employer qualifies, next you'll need to figure out which types of student loans are eligible for forgiveness.

The program requires that borrowers have federal direct loans. This would include loans issued under the William D. Ford Direct Loan Program, specifically Direct Subsidized Loans, Direct Unsubsidized Loans, Direct PLUS Loans and Direct Consolidation Loans. Federal Family Education Loans (FFEL) and Federal Perkins Loans are not eligible unless they are consolidated into a new Direct Consolidation Loan. Private student loans are not eligible for the PSLF program.

If you're unsure of what types of loans you have, be sure to check your loan service provider's website, where you should be able to find a description of each loan you currently have on file.

When Are Loans Forgiven?

Under the program, borrowers who have made 120 qualifying monthly payments under a qualifying repayment plan while employed in a full-time public service job may have the balance of the principal and interest due on their loans forgiven.1 Note that borrowers can receive credit for only one payment per month, and those payments must be received on time.

Changing jobs is part of the modern career track, and with that it's important to know that qualifying payments are cumulative, not consecutive. That means you can switch from a qualifying employer to a non-qualifying employer and back again and not lose the qualifying payments you've made in the past.

One final note regarding Direct Consolidated Loans: It is important to know that the 120-payment counter resets once loans are consolidated. So, while consolidation can make life significantly easier, it could take away progress you have made toward your 120 qualifying payments.

How Much Will You Pay?

In order to take advantage of the PSLF program, you must use one of five Income-Driven Repayment (IDR) plans set forth by the federal government. These plans are designed to make student loan repayment more manageable by decreasing a borrower's monthly payment amount. Payments will be based on a percentage of your discretionary income and will consider your adjusted gross income, family size and total eligible federal student loan balance.

The qualifying IDR plans include:

- Income-Contingent Repayment Plan (ICR)
- Income-Based Repayment Plan (IBR)
- Income-Based Repayment (IBR) for New Borrowers
- Pay As You Earn Repayment Plan (PAYE)
- Revised Pay As You Earn Repayment Plan (REPAYE)

Details for each of these plans can be found at studentaid.gov/app/ibrInstructions.action.

Keep in mind that while these plans are designed to make student loan payments more manageable, in some cases your monthly payment may increase. If this ends up being the case, borrowers should carefully weigh their options and consider how higher monthly payments will affect their short-term cash flow as well as their long-term financial goals.

Strategies for Selecting an IDR Plan

The REPAYE or PAYE plans referenced above may be the best options for borrowers, as payments under these plans equate to 10% of one's discretionary income. What is noteworthy, however, is how discretionary income is calculated under these plans: They take into account a borrower's prior year adjusted gross income as well as a percentage of the borrower's poverty level based on the borrower's state and family size.

When selecting an IDR plan, it is important to note that spousal income may be included in the borrower's discretionary income, which could lead to a higher monthly payment. One cannot exclude spousal income under the REPAYE plan. However, under the PAYE and both IBR plans, borrowers can exclude spousal income from discretionary income by electing to file their taxes as Married Filing Separately. Of course, while this may help borrowers decrease their monthly payments and contribute to the overall forgiveness of their student loans, it's important to consider how filing taxes separately will affect tax liability. An experienced financial professional and/or CPA can provide a cost-benefit analysis based on these options.

Loan Forgiveness Under the CARES Act

Lastly, it's important to remember that through the recently enacted CARES Act, those who have loans held by the federal government will be able to defer their payments until September 30, 2020. Additionally, no interest will accrue during this period. However, as part of our discussion of the PSLF program, it's important to note that the months during which a payment isn't required will still count toward your forgiveness requirements.2

Conclusion

The repayment of student loan debt doesn't come easy for many of us. This debt burden is something that we accrue over several years of education and usually have to pay down over several more years during our working careers. While paying down these debts can take time, programs like the PSLF – in addition to simply understanding your options – are key to shortening the repayment period and easing the burden as much as possible.

For more information, please visit janushenderson.com.

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C-0620-31141 06-30-21