A Primer on Medical Student Loan Repayment Options

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Whether you are a resident, fellow or attending physician, life comes at you fast and the temptation exists to make quick and reasonable, if not optimum, financial decisions. After all, there's only so much free time in which to rest, recharge and pursue your passions.

While we have a larger margin for error for financial decisions, such as where we hold our checking account or how much of a deductible to use for our car insurance, deciding upon a repayment plan for student loans should be a well-thought out financial decision. Unfortunately, the maze of loan repayment options, qualification restrictions, loan forgiveness requirements and other considerations can be a daunting one through which to navigate!

What's at Stake?

According to the AAMC[1], in 2016 the median education debt balance for graduates was $190,000. This means that approximately half of the graduates had a larger loan balance. In our experience of working with physicians, many graduates have a significant other who also has student loans – often large loan balances from medical education.

If not handled appropriately, you may cost yourself tens of thousands of dollars in interest payments you otherwise would've saved. Or even worse, you may cost yourself the ability to have your loan balance forgiven. Far worse, a poorly designed repayment plan can severely limit your financial flexibility throughout your lifetime.

Here is a helpful primer on repayment strategies for your medical school loans. I've kept it as high-level as possible to give you a baseline understanding of the important considerations before you make any decisions.

There are several important resources you may call upon for assistance in navigating the loan repayment option maze including: an experienced financial planner, www.finaid.org, www.aamc.org, www.studentaid.gov as well as your university's financial aid department.

Deferment and Forbearance

Before we explore the most-commonly used repayment options, it would be a good idea to cover deferment and forbearance. According to the Dept. of Education, "A deferment or forbearance allows you to temporarily stop making your federal student loan payments or to temporarily reduce the amount you pay."[2]

With a deferment, you are not responsible for paying the interest that accrues on certain loans during the deferral period.

With a forbearance, you are responsible for paying the interest that accrues on all loans during the deferral period.

In either case, the interest payments for which you are responsible are added to your loan principal (capitalized) at the end of the deferment or forbearance period. *Given the typically large student loan balance, it is better to regularly make some payments, even if only interest, to avoid a much larger loan balance when you sign your first full-time contract.*

Additional information on how to qualify for a deferment or forbearance may be found at the following site: https://news.aamc.org/medical-education/article/taking-sting-out-medical-school-debt/

The Standard Repayment Plan

Otherwise known as the Original Payment Plan, you make a fixed payment each month until your loans are paid off – typically within 10 years. If you have the means to use this repayment option, you will pay the least amount of interest of any of the government repayment plans.

If you do not select a repayment plan when it is time to begin making payments, the company servicing your government loan will enter you into the Standard Plan.

With the median student loan balance of $190,000, the monthly payment using this repayment option can cut deeply into one's resident or fellowship salary, however.

If you prefer a lower payment other options exist to soften the blow to your cash flow.

The Graduated Repayment Plan

This plan starts with lower monthly payments than the Standard Plan. The monthly payment increases every two years and is made for up to 10 years. With consolidation loans, the repayment period can be stretched to between 10 and 30 years.

The Extended Repayment Plan

Payments, which may be either fixed or graduated, may be made over a period of up to 25 years. Due to the longer payment period, monthly payments will be lower than under the Standard and Graduated Plans. The total interest paid over the course of the loan will be higher, however.

Income-Driven Repayment Plans

So, what if you want to make payments now, to cover your interest and keep your debt from snowballing further, but not as much as you would pay using the Standard Plan?

Four income-driven repayment options exist which provide a high degree of flexibility:

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

These options, created by the federal government, allow you to base your payment on 10% to 20% of your discretionary income rather than the size of your loan. Discretionary income is defined as the difference between adjusted gross income (AGI) and 150% of the federal poverty line that corresponds to your family size and the state in which you reside. For example, in 2018 the poverty line for a family of two is $16,460. For a single person, the poverty line is $12,140. The poverty guidelines are maintained by the U.S. Dept. of Health and Human Services and are available at https://aspe.hhs.gov/poverty-guidelines.

The Dept. of Education publishes a very helpful information on income-driven repayment plans at https://studentaid.ed.gov/sa/repay-loans/understand/plans/income-driven

Loan Forgiveness

In 2007, Public Service Loan Forgiveness (PSLF) was created to help ease the financial pressure of large student loans for certain professionals involved in public service. After making 10 years of qualified payments, having worked for a qualified employer, one's remaining student loan balance may be completely wiped out. This is a huge financial benefit and, since it is a taxpayer-funded program, there will be a few hoops to jump through to qualify for loan forgiveness:

Criteria #1: Qualifying Employer. You need to have worked full-time for a qualifying employer – typically a non-profit, the military or in public education. The PSLF candidate will need to annually submit a form from their employer certifying their employment.

Criteria #2: 120 Qualifying Months of Payments. 10 years of qualifying monthly payments is required. If you have multiple loans, only one payment per month counts. Only certain types of loans qualify. For instance, the Federal Perkins Loan and Federal Family Education Loan (FFEL) do not qualify (these can be wrapped up into a consolidation loan but that's a topic of another discussion; suffice it to say, qualifying for PSLF is not a simple process).

Criteria #3: Qualifying Repayment Plan. The qualifying repayment plans are: the Standard Plan or one of the Income-Driven Plans. Using the Standard Plan doesn't make sense as it results in paying off your loans over a ten-year period. If you are applying for loan forgiveness, you want to have a balance that could be paid off after 10 years. So practically you will use one of the Income-Driven Plans such as PAYE (Pay As You Earn) or REPAYE (Revised Pay As You Earn). More on these plans later.

If you are interested in qualifying for PSLF, it is critically important to avoid making a loan repayment decision that results in some or all of the monthly loan payments being disqualified.

If you are not considering PSLF, then you have a much higher degree of flexibility in structuring your loan repayment design.

Loan Consolidation

Who doesn't appreciate simplicity? In fact, it is a relief when we have a service experience that involves one or no actions on our part.

Consolidating multiple government loans into one Direct Consolidation Loan creates simplicity as you only need to write one monthly check. It also may lower your interest rate. The new fixed rate is equal to the weighted average rate of the loans being consolidated rounded up to the nearest 1/8%.

Be very careful: if you consolidate multiple government loans into the same loan, but do so after you began making payments, you've wiped out the credit you've earned towards the 10 years of qualifying payments.

You may apply for loan consolidation at the Dept. of Education's student aid site: https://studentaid.ed.gov/sa/repay-loans/consolidation#should-i

Refinance

There are two primary reasons why you may want to refinance your student loans: to lower your Interest rates and to create a custom loan repayment period.

Refinancing your loans at a lower interest rate, if available, may save you a considerable amount of interest.

Perhaps you and your financial planner has created a financial plan and, given your unique goals (saving for a home down payment, saving for a child's college, saving for retirement, etc…), it would be in your best interest to create a custom repayment period.

A private lender can help you create a customized repayment plan using fixed or variable rates and a stated repayment period.

However, before you refinance your loans, be very careful to consider that doing so would disqualify you from loan forgiveness and from using the aforementioned government loan repayment options.

Questions to Ask

Deciding upon a loan repayment design is one of the most critically important financial decisions you will make during your lifetime. Some questions to ask yourself are: Is my goal to minimize the amount of cumulative interest I pay on my student loans? Or is it to keep my payments low for a period while my income ramps up? Do I want to keep open the ability to qualify for loan forgives?

There is a lot of information out there about loans and repayment plans. Perhaps that's the biggest challenge – too many options. This primer has provided you with the basic information you need to begin to craft your repayment plan. If you would benefit from a personal consultation, please contact our office.

[1] https://news.aamc.org/medical-education/article/taking-sting-out-medical-school-debt/

[2] https://studentaid.ed.gov/sa/repay-loans/deferment-forbearance

Which student loan repayment plan works best for you and your life goals?

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Eric is a managing partner of the independent wealth management practice, Wealth Impact Advisors, LLC. He has provided financial guidance to medical professionals, business owners and families for over two decades. He is proud to serve clients in a fiduciary capacity as a CERTIFIED FINANCIAL PLANNER™ practitioner and an Accredited Investment Fiduciary®.

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