

Understanding Education Loans

Types of Education Loans

Loans are a reality for most college students who receive financial aid. Unlike scholarships and grants, loans must be repaid after graduation – there are even some loans that require that repayment begin immediately upon receiving the loan. Certainly you should look for grants or scholarships (“free money”) before you borrow, but, if you do borrow, understanding the different loan types will help you save money in the long run.

Federal loans for education are the best place to start. The interest rate generally will be lower and there are often ways to reduce the amount you pay. The repayment period for student loans doesn’t usually begin until after you leave college and lasts for at least 10 years. There are federal loans for parents too. These loans are available through the U.S. Department of Education’s Direct Loan Program. Talk with your college or university admissions office about how to apply.

The first step in applying for these federal loans will be the completion of the Free Application for Federal Student Aid (FAFSA) which determines your need for state and federal financial aid. Here’s a brief overview of the major loan terms and concepts:

Direct Subsidized Loans – Awarded to financially needy students based on their Expected Family Contribution (EFC) and the cost of attendance of a particular school. Interest is not charged until graduation or dropping below a half-time course schedule. In the meantime, the federal government “subsidizes” the loan by paying the interest. Subsidized loans may not be used towards the EFC.

Direct Unsubsidized Loans – Student borrowers with no financial need are eligible for Direct Unsubsidized Loans. Interest on these loans is not paid by the federal government and is the responsibility of the student at all times. Borrowers can either pay the interest while they are enrolled or have it added to the loan principal. Unsubsidized loans can be used to help pay the Expected Family Contribution (EFC).



Federal Consolidation Loans – A Federal Consolidation Loan allows a borrower to consolidate several types of federal education loans with various repayment schedules into one loan. This simplifies the repayment process, because you make only one payment per month.

Loans being consolidated must be federal, not private loans that were made to the borrower who is applying for the Consolidation Loan. The interest rate and payments on the new Consolidation Loan may be lower, but the extended repayment period increases the total interest charges over the life of the loan.

Alternative or Private Loans – Loans made available from nonprofit lenders, banks, colleges, universities, and other lenders that do not rely on the federal government as a guarantor. These loans may have a higher interest rate than federal loans. But if you have borrowed the maximum amount through federal loans and still need more, a private loan can help cover your cost of attendance. Just be careful – some private or alternative loans do not require certification by the college financial aid office. If a lender makes it too easy to receive large loans, you may get into financial trouble.

Borrowing a private loan that your school must certify can help limit the amount you borrow. Since it will be your responsibility to pay both federal and alternative loans back, you will want to be conscious of and carefully consider your total indebtedness.

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