

Managing Your Federal Student Loans

Current Relief Creates Planning Opportunities



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On January 20, 2021, President Biden extended the suspension of federal student loan payments without penalty or interest until September 30, 2021. This relief is intended to help borrowers recover from the economic impact of the pandemic, especially those who experienced a reduction in income. If your monthly cash flow is still in good shape, take advantage of this suspension to make progress on your financial goals.

Where Should I Redirect My Federal Student Loan Payments?

Nine months without student loan payments means a potential influx in discretionary income. Depending on where you're at in your financial journey, you might consider using this money to:



Should I Make Payments Anyway?

If your other debt isn't significant, and you're satisfied with your savings levels, you might decide to keep making payments. Continuing to pay off your loans will directly reduce the outstanding principal balance since no interest is accruing. You can also target payments towards specific loans, like those with higher interest rates, as you don't have to make minimum payments on each separate loan. As an added benefit, making timely payments can help build and potentially improve your credit score.

Should I Refinance My Federal Student Loans?

Refinancing federal student debt may also be appropriate in some cases. If your income is relatively secure and you have cash reserves to tide you through any potential job loss, refinancing may be a good option. Depending on your outstanding debt balance, the interest savings could outweigh any possible changes to loan forgiveness terms in the future.

For example, a \$250,000 balance at 6% over 15 years compared to 3% over 15 years equates to interest savings of roughly \$68,975. This savings is more than the proposed forgiveness amounts, not to mention many borrowers with increasing income likely won't qualify to have their loans discharged.



Of course, every situation is unique. You need to weigh the pros and cons of refinancing as you would any financial decision. Keep these important caveats in mind as you consider your options. First, be cautious of low but potentially variable interest rates. Fluctuating rates could easily reduce the benefit of refinancing. Opting for a variable rate may not be wise unless you plan to pay off the loan quickly. Second, if you refinance your federal student loans with a private lender, you'll lose access to certain benefits, including the income-driven repayment plan and existing loan forgiveness programs. If you know you won't qualify for these programs, refinancing may make sense. Otherwise, you'll have to decide if the potentially lower interest rate is worth the trade-offs.

What Happens if My Loans are Forgiven?

Loan forgiveness has captured the attention of the media, President Biden, Congress and the millions of borrowers with outstanding balances. Historically, borrowers had to report the discharge of student loan debt as taxable income. For example, loan forgiveness of \$10,000 would result in a tax liability of approximately \$2,200 come April 15 for someone in the 22% tax bracket. While this amount is much cheaper than the loan repayment, it can come as an unwelcome surprise, especially if you don't have the cash reserves to cover it.

Lawmakers have recognized the undesirable tax consequences widespread student loan forgiveness could have on those most affected by the pandemic. As a result, The American Rescue Plan Act, signed into law on March 11, 2021, includes a provision that makes any discharge of federal student loan debt through December 31, 2025 tax-free. This provision gives Congress more flexibility as they debate and negotiate the various proposals on the table, including a one-time \$10,000 forgiveness and \$50,000 forgiven over five years.

Plan While You Wait

With the possibility of loan forgiveness lurking in the background, it's easy to take a wait-and-see approach. But when it comes to your finances, it's better to be proactive than reactive. Cerity Partners planning specialists can help you understand your federal student loan repayment options, model different scenarios and create a plan that can be "switched on" based on future legislative developments.

Contact a Cerity Partners advisor to begin the conversation. For more financial planning insights, visit the [thought leadership section](#) of ceritypartners.com.

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