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Personal Finance
Student Loan Fact Sheet Series

Recovering from Student Loan Default

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Failing to make regularly scheduled student loan payments can have a very negative effect on a consumer's life. Federal loan servicers report delinquencies of at least 90 days to the three major credit bureaus (Equifax, Experian, and TransUnion). Default occurs when an individual fails to make a student loan payment for more than 270 days. For private loans, each lender will have different rules. This fact sheet will focus on rules regarding federal student loans.

Consequences of Default

The consequences of student loan default can be financially devastating. Below is a list of default consequences as stated on the Federal Student Aid website (https://studentaid.ed.gov/sa/repay-loans/default).

- The entire balance of your loan and interest is immediately due and payable.
- You lose eligibility for deferment, forbearance, and repayment plans.
- You lose eligibility for additional federal student aid.
- Your loan account is assigned to a collection agency.
- The loan will be reported as delinquent to credit bureaus, damaging your credit rating.
- Your federal and state tax refunds may be intercepted and used to repay debt.
- Your student loan debt will increase because of late fees, additional interest, court costs, collection fees, attorney's fees, and other costs associated with the collection process.
- Your employer can garnish your wages.
- The loan holder can take legal action against you, and you may not be able to purchase or sell assets such as real estate.
- Federal employees face the possibility of having 15% of their disposable pay reduced by their employer to pay back student loan debt.
- It will take years to reestablish your credit and recover from default.

Avoiding Default

If you are having difficulty making student loan payments, it is essential to be proactive and avoid going into default. By contacting your loan servicer, you may be able to switch repayment plans, change your payment due date, or get a deferment or forbearance.

A deferment is a postponement of payment on your loan that is allowed under certain circumstances. Interest on Subsidized loans is also postponed. You qualify for a deferment in the following situations:

- During a period of at least half-time enrollment in college or career school.
- During a period of study in an approved graduate fellowship program or in an approved rehabilitation training program for the disabled.
- During a period of unemployment or inability to find full-time employment (up to 3 years).
- For Perkins Loans, during a period of service qualifying for Perkins Loan discharge/cancellation.
- During a period of economic hardship (as defined by the Department of Education).
- During Peace Corps service (for up to 3 years).
- During a period of active duty military service during a war, military operation, or national emergency.
- During the 13 months following the conclusion of qualifying active duty military service.

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Forbearance is a way to postpone your payments for up to 12 months if you do not qualify for a deferment under one of the conditions listed above. Interest still accrues on all loans during a forbearance period. There are two types of forbearances: discretionary and mandatory.

In a discretionary forbearance, your lender decides whether to grant it or not. You can request a discretionary forbearance for financial hardship or illness.

A forbearance which your lender is required to grant is called a mandatory forbearance. You can request a mandatory forbearance for the following reasons:

- Serving in a medical or dental internship or residency program, and you meet specific requirements.
- The total amount you owe each month for all the student loans you received is 20% or more of your total monthly gross income.
- Serving in a national service position for which you received a national service award.
- Performing teaching services that would qualify for teacher loan forgiveness.
- Qualifying for partial repayment of your loans under the U.S. Department of Defense Student Loan Repayment Program.
- You are a member of the National Guard and have been activated by a governor, but you are not eligible for a military deferment.

Getting Out of Default

When borrowers default on their federal student loans, they have three options: loan repayment, loan rehabilitation, and loan consolidation.

Loan Repayment

One option for getting out of default is to repay the full amount of your defaulted student loan. Perhaps from a large lump sum such as a tax refund or an inheritance.

Loan Rehabilitation

To rehabilitate your loan, you must contact the Department of Education and agree upon a payment amount and make nine full payments. Payments secured on an involuntary basis (wage garnishment, litigation, etc.) do not count toward the nine payments. Once you have made the payments (within 20 days of their monthly due dates) your loans will no longer be considered to be in default status. You can rehabilitate a defaulted loan only once.

Loan Consolidation

A third option is to consolidate your federal student loans. A defaulted loan may be included in a consolidation loan after you make satisfactory repayment arrangements on the defaulted loans with the current loan holder or you agree to repay the new Direct Consolidation Loan under either the Income Contingent or Income-Based Repayment Plans.

Resources

eXtension Student Loans: http://articles.extension.org/pages/72895/student-loans

Federal Student Aid: https://studentaid.ed.gov/sa/

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