For college bound, a look at financial aid changes

By Candice Choi, Associated Press

NEW YORK – The mad dash to cobble together money to pay for college will soon be under way.

In the weeks ahead, colleges will begin mailing out their much-anticipated acceptance letters and financial aid packages. The notices will finally give high school seniors a clearer idea of what their futures will hold.

But amid all the emotion, students and families will need to start figuring out how they'll pay for tuition. The average bill now comes in at more than $17,000 for an in-state student at a public college.

- Navigating the universe of financial aid can be confusing. That's because there's a vast patchwork of grants, scholarships and loans available. But failure to properly compare the options and explore alternatives could mean a difference of thousands of dollars in debt upon graduation.

Adding to the confusion: Recent talk of changes in financial aid. Here's a look at the process, and what's behind the possible changes:

Comparing costs

As part of his broad plan to make higher education more affordable, President Obama recently said he wants to make it easier for families to size up the cost of college.

As it stands, there isn't a uniform template for financial aid award letters and officials say the forms can be difficult to decipher, even misleading. For example, schools usually provide a total "out of pocket" cost after subtracting aid such as grants and scholarships. But some schools also subtract loans from that figure, even though loans have to be repaid and actually push up costs because of interest charges.

In other cases, interest rates and other loan terms are not spelled out. Officials say this could lead to students taking on more debt than they realize.

To address the issue, the Department of Education and the newly created Consumer Financial Protection Bureau announced in October that they are developing a model financial aid form. There aren't any plans yet to make the form mandatory. But once a template is final, Congress could vote to require colleges to use it to maintain access to federal aid. The adoption of such a form has also been widely supported by student advocates.

Separately, Obama is pushing for a "college scorecard" that would require schools to disclose their graduation rates, rate of employment and debt repayment among graduates.

Interest rates

Taking out a student loan to attend college has become the norm, with two-thirds of graduates leaving campus in debt. But not all loans are alike. So it might have caught your attention last month when Obama said in his State of the Union address that the fixed interest rates on student loans are set to double in July if Congress fails to act.

Before you panic, keep in mind that there are primarily two types of federal student loans: subsidized and unsubsidized. The difference is that the government doesn't start charging interest on subsidized loans until the student graduates. With unsubsidized loans, interest starts accruing right away.

The loans also come with different interest rates. Unsubsidized loans currently charge a fixed rate of 6.8%. The interest rate on subsidized loans was gradually lowered to its current fixed rate of 3.4% over the past few years. But the law that temporarily reduced the rate is scheduled to expire in July.

So unless Congress extends the reduction, the rate on subsidized loans will snap back to 6.8%.

This may affect even families that are relatively well off; not everyone who qualifies for a subsidized loan is from a low-income household. This could be the case for students who are attending expensive schools or have other siblings in college. Eligibility is based on financial need, which is determined by a formula on the Free Application for Federal Student Aid.

Then there are private student loans, which come with entirely different terms. These are widely considered an option of last resort since the interest rates tend to be higher and variable, meaning they rise and fall with a benchmark rate. And since benchmark rates are at record lows, the rates of private lenders are likely to rise in years ahead.

Hardship clauses

Another difference to note between private and federal loans is that the latter come with greater safety nets.

The issue came to light last week when Sallie Mae, a private student lender, said it was changing how it handles a fee it charges unemployed borrowers who want to suspend payments.

Sallie Mae isn't cancelling the $50 fee, but said it will now apply the money toward the borrower's loan balance if on-time payments are resumed for six months in a row. The change came after an online petition asking the company to drop the fee collected more than 77,000 signatures on Change.org.

By contrast, borrowers who are unemployed or suffering economic hardship aren't charged to defer payments on federal student loans.

In addition, they can apply for a program called Income-Based Repayment, which caps monthly payments at 15% of annual income above $16,300. Those who earn less don't have to make any payments; any remaining debt after 25 years is forgiven, or after 10 years for those entering public service jobs.

For borrowers who take out at least one federal loan this year, the cap on monthly payments will be lowered to 10% of income above $16,300. Borrowers will also be relieved of payments sooner, with any remaining debt forgiven after 20 years.