

## SAVED BY THE BELL: CONSOLIDATING COLLEGE LOANS

The school-loan bell is about to ring and you don't want to be late.

Graduated or soon-to-graduate college students with sizable education loans may want to consider consolidating their loans by July 1, 2005. Historically low interest rates and the potential for dramatic changes in the federal government's student loan consolidation program may make this the last best time to grab a consolidation loan before the bell rings.

Here's how the federal consolidation loan program currently works. Students with multiple federally backed loans such as Perkins and Stafford loans can consolidate those loans into a single fixed-rate loan. (Private loans cannot be consolidated under this program, and loans already consolidated cannot be reconsolidated.) The rate is based on the weighted average of the consolidated loans, rounded up to the nearest one-eighth of a percent. Depending on the weighting, the consolidated rate may not necessarily be lower than the effective combined rate of the consolidated loans, but it probably will be.

Until July 1, 2005, consolidation rates go as low as 2.77 percent for students who consolidate their loans while they're still in school or within a six-month grace period immediately following graduation or leaving school. Students who don't consolidate until after the grace period pay a 0.6 percent higher interest rate—currently as low as 3.37 percent. In addition, some private lenders will reduce loan rates even further if you agree to automatic deductions from your checking account or you make on-time payments for a designated period.

Beyond potentially lowering the overall interest rate and saving hundreds or thousands of dollars in interest charges, borrowers benefit from consolidation in three other ways. First, they replace multiple payments, and paperwork, with a single monthly payment.

Second, and often the biggest benefit, is that consolidation allows borrowers to stretch out their loan payments for longer than the standard 10 years—as long as 30 years, depending on the size of the loan. This means smaller monthly payments, a big help for recent graduates working in relatively low-paying starter jobs.

Third, consolidation loans allow the flexibility of prepaying penalty free, which you might be able to afford once you move into a higher-paying job.

The incentive to consolidate by July 1 stems from several factors. First, consolidation rates are at record lows as the nation's overall interest rates have hit historical lows. But short-term interest rates have started to rise again, so consolidation rates are expected to go up when new annual rates are announced July 1.

Another factor is the potential for the consolidation program itself to change. Private

lenders who actually issue these loans have been lobbying to change the consolidation rates from fixed to variable—rates that could go as high as 8.25 percent. The Bush administration's proposed 2006 federal budget includes just such a recommendation. In a rising interest-rate environment, variable rates could add thousands of dollars in finance charges for some borrowers.

The Bush proposal would also add a 1 percent consolidation fee the borrower would have to pay and would double the fee the government charges lenders for originating the loans. Lenders would likely try to recoup those costs, possibly lowering or eliminating some of the loan-reduction incentives they currently give borrowers.

In light of the almost certain interest-rate hike, and the possible changes in the very heart of the program itself, consolidating education loans soon may be a smart move. But consolidating loans isn't for everyone.

Stretching out payments beyond ten years, for example, usually means borrowers pay more in total interest than if they pay the loan off in ten years. Lower consolidated payments may make you feel you can pile on new debt, compounding the problem.

Additionally, some student loans, such as Perkins, can be partially or completely forgiven for some graduates, such as teachers who work in low-income schools—but the loan cannot be forgiven if it is consolidated.

Moreover, if you've managed to pay your unconsolidated loans on time for close to 24 or 48 months, it might be wise to not consolidate. Why? Because some lenders will reduce interest rates for the remaining loan period by as much as two percent.

Whatever you do, don't miss the bus.