Private Student Loans - What to Know Before You Borrow

Your Rights and Responsibilities

Before you borrow any money, you should clearly understand all aspects of what is expected of you and what rights you have as a borrower.

What is a Private Student Loan?

Private student loans, also known as private education loans, alternative loans, or alternative student loans, are unsecured, credit-based loans offered by banks and credits unions which may be used to help "bridge the gap" between the financial aid students have been awarded and any additional amount they feel may be needed to help achieve their educational goals. When considering a private student loan, it is extremely important that you first exhaust ALL other financing options such as grants, scholarships, and federal student loans.

A private student loan may be a wiser financial decision than using credit cards or home equity lines of credit. However, it is ultimately the responsibility and choice of the borrower (and co-signer, if needed) to make the best personal financial decision.

Loan Limits

The maximum loan you may borrow is limited to your “cost of attendance” less other financial aid received. You should never borrow more than you need. You will have to apply each academic year for a private loan. It is recommended that the same lender be used each year unless circumstances dictate otherwise.

Choosing a Lender

During the online application process you will be able to view a chart that contains lenders that Hampden-Sydney students have used in the past. You will be able to compare loan products and also make alternate lender choices. Hampden-Sydney College does not discriminate against any lender and will certify a loan for any lender you choose.

Understanding Your Private Loan Interest Rate

Interest rates on private student loans can be "variable" or "fixed". Variable Interest Rate is defined as the interest rate on a loan that rises and falls based on the movement of an underlying index of interest rates. For example, many credit cards charge variable interest rates, based on a specific spread over the prime rate. Most home equity loans charge variable rates tied to the prime rate, also called adjustable interest rate. Fixed Interest Rate is defined as the interest rate on a loan or mortgage that will remain at a predetermined rate for the entire term of the loan.

Interest begins accruing as soon as your loan is disbursed and will continue to accrue until the loan is paid in full. The interest on private loans is predominantly “simple interest,” meaning that interest does not accrue on interest, only on the principal balance. Credit cards are an example of “compound interest,” where interest accrues on both your principal balance and the interest that you have already accrued.

What is a Credit Reporting Agency?

A credit reporting agency (also called credit bureau) gathers a consumer’s credit history into a brief summary. Lenders use this report as the basis for determining if they will extend credit. The three major credit reporting agencies are:

- Equifax, 800-685-1111 www.equifax.com
- Experian, 888-397-3742 www.experian.com
- Trans Union, 800-916-8800 www.transunion.com

Your credit score is like a snapshot of your level of credit risk at a particular point-in-time; when your credit information changes, so does your credit score. To give yourself the credit you deserve, pay your bills on time, pay down any outstanding debt and avoid taking on new debt or applying for too many new credit cards.

What is Credit Ready vs. Credit Worthy?

Someone who is creditworthy has been determined to have the ability to repay the loan based on their credit history. Factors in the evaluation may include a minimum monthly income, previous credit experience, credit report and credit score. Someone who is credit ready has no negative credit history. Lenders may lend to a person who is only credit ready based on some other statistical data showing they will have the ability to pay in the future (i.e. future college graduate).

What is Credit Scoring?

Lenders use credit scoring to make fast and objective decisions on which applicants are likely to repay their loans on time. Credit scoring is calculated using many pieces of your past bill payment history (i.e. number and types of accounts, late payments, outstanding debt, the age of your accounts). The way you have handled your credit in the past is often a good indication of how you will manage credit in the future. Therefore, your credit score is like a snapshot of your level of credit risk at a particular point in time and is predictive of your future credit performance.

Do I Need a Co-Signer to Apply for a Private Student Loan?

Most students will need to apply with a credit-worthy co-signer in order to obtain a private student loan. College students generally don't have a long-standing credit history, or significant income, and most lenders are unwilling to give money under these circumstances.

Even if you have enough income and credit history to be approved for private student loans on your own, using a co-signer may help you improve your loan terms. Private student loans with a co-signer generally have lower interest rates and better terms than when a student applies on his own.

Many lenders now offer a "co-signer release" option which, after a certain number of consecutive, on-time payments have been made, releases the co-signer from the loan.

Repayment Period

The repayment period may vary depending on the lender and the loan. The longer the term of the loan, the lower the monthly payment although you may pay more interest than if the term is smaller. If educational costs require you to borrow large amounts, you may want to consider a loan that offers a longer repayment term.

Repayment Incentives

Some lenders offer incentives in the form of a lower interest rate. For example, if you sign up for ACH or a direct debit from your bank account, they will reduce the interest rate on your loan.

Repayment

It is highly recommended that you pay down your loans as quickly as possible. This will reduce the amount of interest you will pay over the life of the loan. All loans should allow you to prepay all or a portion of your principal and/or interest at any time without penalty.

It is important to avoid delinquency and default. So if you have trouble making any scheduled payment, be sure to contact your loan servicer for assistance. Ask about payment deferral or forbearance options.

Interest Capitalization

If you choose not to pay the interest on your loan while you are in school, the interest may be capitalized (added to your principal balance). Different lenders capitalize interest at different times. Some lenders will capitalize interest quarterly, annually or at repayment. If the interest is capitalized quarterly or annually, the loan is more expensive than if it is capitalized only once at repayment.