Participant Guide

PAYING FOR COLLEGE AND CARS

FDIC Money Smart for Young Adults

Building: Knowledge, Security, Confidence

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Your Guides

Students from Lakeview High are going to be your guides in this lesson.

Jasmine

Hobbies: Hanging out with friends, shopping, collecting teddy bears
School life: Likes English class, swims on the swim team
Job: Works weekends and holidays at her aunt's gift shop
Family: Younger brother named Dominique, large extended family
Future plans: Go to an in-state college and become an exercise physiologist

Todd

Personality: Shy, good sense of humor, intelligent
School life: Likes school, but does not work very hard at it
Jobs: Two part-time jobs (fast food and a grocery store)
Family: Mom and sister
Future plans: Attend college; he is not sure where he wants to go or how he will pay for it, but is saving all he can

Ramón

Hobbies: Going to the movies or playing mini golf with his girlfriend
School life: Plays on the soccer team
Family: Born in the United States (U.S.), but his parents are from Peru; he has a little sister and an older brother who is a pilot in the Air Force
Job: Repairing computers; wants to work for NASA some day
Future plans: Attend college on a soccer scholarship to study engineering

Grace

Hobbies: Art, drawing fashion sketches
School life: Does not really fit into the "high school scene"
Family: Two parents, no siblings
Job: Works at a clothing store at the mall
Future plans: Enroll in Fashion Design School

Checking In

Welcome

Welcome to *Paying for College and Cars*! Understanding installment loans and student loans is important when using loans to make purchases and pay for college. This training will help you understand what installment loans and student loans are all about.

Purpose

The *Paying for College and Cars* module provides general information about installment loans, including car loans and student loans. When you have completed this module, you will be able to describe the characteristics of consumer installment loans and be able to choose what student loans are best for you to use.

Objectives

After completing this module, you will be able to:

- Differentiate between secured and unsecured installment loans.
- Identify the factors lenders use to make loan decisions.
- Identify the questions to ask when purchasing a car.
- Describe various types of college loans and loan programs.

Student Materials

You have a copy of the *Paying for College and Cars* Participant Guide. You can take it home and use it as a reference. It contains:

- Information and activities to help you learn the material
- Tools and instructions to complete the activities
- Checklists and tip sheets
- A glossary of the terms used in this module

Pre-Assessment

1. What is a secured loan?
    a. A loan in which you pledge collateral (something of value like a house or car) to the lender
    b. A loan where no collateral is needed
    c. A low interest-rate loan
    d. A loan that can be approved quickly

2. When you finance a car, the car then becomes ___________ for the loan.
    a. Payment
    b. Credit
    c. Collateral
    d. The title

3. Which of the following should you consider when deciding on whether to finance or lease a car?
    a. Wear and tear
    b. Monthly payments
    c. Mileage limitations
    d. All of the above

4. What is the first step in applying for financial aid?
    a. Talk with you financial advisor
    b. Complete the Free Application for Federal Student Aid (FAFSA)
    c. Apply to a college
    d. Calculate the cost of college

5. Which of the following describe an installment loan? Select all that apply.
    a. A loan that is repaid in equal amounts
    b. A loan that is repaid in varying amounts
    c. A loan that must be repaid in a specific period of time (e.g., 5 years)
    d. An open line of credit or loan that is not limited to a specific period of time

6. Unsecured installment loans are generally used to pay for:
   a. Cars
   b. Education
   c. Home
   d. Furniture or computers purchased through store financing or rent-to-own services

7. _______ is the dollar amount the loan will cost, including interest, service charges, and loan fees.
   a. Annual Percentage Rate (APR)
   b. Finance charge
   c. Collateral
   d. Pre-approval

8. Which of the following refers to how you have paid bills or debts in the past? This is one of the Four Cs lenders use to determine whether to grant you a loan.
   a. Capacity
   b. Capital
   c. Character
   d. Collateral

9. Where can you obtain a car loan?
   a. Banks/thrifts
   b. Credit unions
   c. Car dealerships
   d. Finance companies
   e. All the above

10. When comparing loans, you should choose the loan:
    a. With the lowest monthly payment
    b. With the lowest APR
    c. That covers the entire cost so you do not have to make a down payment
    d. With a longer term (e.g., 7 years) so the payments will be more affordable

11. Which of the following need to be paid back (with interest) after you finish or leave school?
    a. Scholarships
    b. Grants
    c. Federal student loans
    d. Federal Work-Study (FWS) earnings

12. Which of the following might you receive if you fit a particular profile (e.g., hold a high grade point average or have a special talent in athletics or in music)?
    a. Scholarships
    b. Grants
    c. Federal student loans
    d. Federal Work-Study (FWS) loan

13. In addition to tuition, what are some other costs associated with going to college?
    a. Books and supplies
    b. Food and housing
    c. Personal and medical expenses
    d. All of the above

14. What is a car title loan?
    a. A low-interest rate loan
    b. A short-term loan (e.g., 1 month) that allows you to use your car as collateral
    c. A longer term loan (e.g., 3–5 years) that allows you to purchase a car
    d. A loan that allows you to combine debts into a single loan

Installment Loan Basics

You can see that Todd and Ramón are both finding out that college is going to be very expensive. Even though Ramón has a scholarship, he will soon find out that there will be many other items and services to pay for when he goes to college. What are some ways Todd and Ramón can pay for college and other expenses? What is the difference between a scholarship and a loan?

What is an Installment Loan?

Generally an installment loan is when you borrow a set amount of money and repay it in fixed monthly payments, or installments, for a specific period of time. These loans are usually repaid over several years.

An installment loan is different from open-end credit (e.g., credit cards). With open-end credit, the lender allows you to borrow against a preapproved credit line. Therefore, your payments depend on how much you borrow.

Types of Installment Loans

There are two types of installment loans:

- Secured loans
- Unsecured loans

Secured Installment Loans

A secured installment loan is one in which you offer collateral for the loan. You must give up the collateral to the lender if the loan is not paid back as agreed.

The interest rates for secured installment loans are comparatively lower than unsecured loans.

A car loan is an example of a secured installment loan.

Collateral

Collateral is security you provide a lender. Giving the lender collateral means that you pledge an asset (e.g., your car) to the lender with the agreement that the lender can take it to help repay the loan if you do not make payments as agreed.

Generally if the collateral is not enough to repay your loan, you are still responsible for the remaining loan balance and other costs.

For example, if you do not make payments on the loan for your car, the lender can repossess (take away) the car. The lender will then try to sell the car. You will have to pay any difference between how much the car sells for and what you owe on the loan (plus fees and interest).

Unsecured Installment Loans

An unsecured installment loan is a loan that is not secured by collateral. An example of an unsecured installment loan is a student loan.

Loan Tips

When getting a loan:

- Beware of companies and websites that charge high rates and application fees. Look for hidden charges.
- Shop around. Compare offers.

Activity 1: Cost of Installment Loans

There are four terms to keep in mind when looking at installment loans:

- Annual percentage rate (APR)
- Fixed-rate loan
- Variable-rate loan
- Finance charge

Cost Terms

- **APR:** The cost of borrowing money (expressed as a percentage rate) on a yearly basis. When shopping for the best loan rates, compare the APRs rather than the interest rates because APRs reflect both the interest you are charged and any fees. This is the single most important tool to use when comparing loan offers and advertisements.

- **Fixed-rate loan:** A loan that has an interest rate that stays the same throughout the term of the loan. Most installment loans have fixed rates.
- **Variable-rate loan:** A loan that has an interest rate that might change during any period of the loan, as written in the loan agreement or contract.
- **Finance charge:** The dollar amount the loan will cost, including: interest, service charges, and loan fees.

Instructions:
Answer each question by identifying the correct cost term.

1. Stephanie took out a car loan with a 10 percent interest rate and paid $100.00 in loan application fees. What rate reflects the interest paid plus the application fee?
2. Michael took out a loan to buy a computer. He must make 24 equal payments over 2 years at 10 percent interest. Which lending term best describes this type of loan?
3. Kevin took out a loan for a car. He must pay $3,000.00 in interest, service charges, and loan fees. What lending term best describes these costs?

Loan Approval

The Four Cs of Loan Decision Making
Lenders generally review the Four Cs to decide whether to grant you a loan. The Four Cs are: capacity, capital, character, and collateral.

- **Capacity** refers to your present and future ability to meet your payment obligations. This includes whether you have enough income to pay your bills and other debts.
- **Capital** refers to the value of your assets and your net worth.
- **Character** refers to how you have paid bills or debts in the past. Your credit report is one tool lenders use to consider your willingness to repay your debts.

- **Collateral** refers to property or assets offered to secure the loan.

Activity 2: Loan Approval

When you are applying for a loan, the loan officer may ask the following questions regarding the Four Cs of Lending.

Capacity

- Do you have a job?
- How much money do you make each month?
- What are your monthly expenses?

Capital

- How much money do you have in your checking and savings accounts?
- Do you have investments or other assets (e.g., a car)?

Character

- Have you had credit in the past?
- How many credit accounts do you have?

Collateral

- Do you have assets to secure the loan beyond your capacity to pay it off?

The following characteristics show that a borrower does not have capacity, capital, character and/or collateral and should not receive a loan:

- Making late payments consistently
- Filing for bankruptcy
- Having property repossessed or foreclosed
- Having a court order requiring a debtor to pay money to the creditor

Car Loans

Where to Get Information

There are many decisions you must make before purchasing or leasing a car.

The Federal Trade Commission (FTC) has many publications that can help you answer these questions so you can get a car at the best price. You can download brochures from the FTC's website (listed in the For Further Information section of your Participant Guide), including:

- *Buying a New Car,* which includes tips on how to choose a car, information on negotiating the price, and considerations when financing a car
- *Buying a Used Car,* which includes information explaining different payment options, dealer sales, private sales, and warranties

Other FTC publications include:

- *Financing a Car*
- *Fueling Up*
- *Leasing a Car*
- *Renting a Car*

To save potentially hundreds or even thousands of dollars, it pays to consult these resources before you go car shopping.

The minimum requirements for obtaining a car loan or lease vary. In general, you and/or the co-qualifier must be at least 18 years of age. The lender will want to make sure you have sufficient income to pay the loan. The lender will also check your credit history and want to know how long you have held your present and past jobs and how long you have been at your current residence, and possibly your past residences.

Car Loans versus Car Leases

There are several factors that you need to consider when deciding between getting a car loan or a car lease, including:

- Ownership potential
- Wear and tear
- Monthly payments
- Mileage limitations
- Auto insurance
- Cost

Activity 3: Car Loans versus Car Leases

It is important to understand the differences and carefully consider all the costs and benefits before deciding whether to buy or lease.

Factors	Car Loans	Car Leases
Ownership potential	• The car belongs to you and the bank that gave you the loan until you have paid off the loan. • Then, the car becomes yours.	• You are essentially renting the car from the dealership. The lease is like a rental agreement. You make monthly payments to the dealership for a set number of months. • The car does not belong to you. When the lease ends, you have to return the car to the dealership. • You may decide to purchase the car at the end of the lease. However, the total cost generally ends up being more than it would have been if you had bought the car.
Wear and tear	• No additional costs for wear and tear are included in your loan agreement.	• Most leases charge you extra money for any damage found at the end of the lease that goes beyond normal wear and tear.
Monthly payments	• Payments are higher, but you only pay them for a set term. Then, you own the car.	• Payments are lower because you are not purchasing the car; the dealership still owns it. • As long as you lease a car, you will continue to make monthly payments.
Mileage limitations	• There are no mileage restrictions.	• Leases restrict the number of miles you can drive the car each year. • If you exceed the mileage allowed, you have to pay the dealer for each mile over the limit according to your lease. • For example, a dealer may charge you $.15 for every mile that you drive over 24,000 miles in 2 years. If you drive the car an additional 3,000 miles, you would owe the

		dealer $450.00 for those miles.
Auto insurance*	• It is usually less expensive than auto insurance for leased cars. • Insurance may cost more during the loan than it will after the loan is repaid because the lender may require more coverage.	• It usually costs more if you lease a car than it does if you buy. • Most car leases require you to carry higher levels of coverage than purchase agreements do. • Some insurance carriers may also consider leasing to be higher risk than purchasing.
Cost	• Purchasing a car is usually more cost effective if you plan to keep the car long term. • However, in the short term, the costs will probably be greater than a car lease because your total loan amount and monthly payments are likely to be higher.	• A lease will probably cost less than a car loan in the short term because your total loan amount and monthly payments are likely to be lower. • However, if you exceed the mileage on a leased car and/or decide to buy it outright once your lease has expired, it will end up costing you more.

*Make sure you find out what the requirements are and get a cost estimate from your insurance company before you decide whether to lease or buy. Remember, you need insurance coverage for your car before you can legally drive it away from the dealership.

Financing My First Car

Characters:

- Big Al, the car salesman
- Jasmine
- Rick, Jasmine’s father
- Narrator

Narrator: Jasmine and Rick are walking around Big Al's Super Used Cars lot and Big Al approaches them as they are looking at a blue sports car.

Al: Hello there, folks! How can I help you this beautiful afternoon?

Rick: Well, my daughter is looking to buy her first car.

Al (looking at Jasmine): Well alright. What type of car are you looking for?

Jasmine: I'd like a car with satellite radio, a navigation system, air conditioning, sun roof….

Rick (cutting off Jasmine): She wants the best deal you have on the lot…she's paying for this car herself!

Jasmine: Yeah, I know I have to pay for it myself, Dad! I really like this blue one! How much is it?

Al: The sticker here says $10,000.00… (*Jasmine sighs and frowns.)*…but I think I could drop that down to $9,250.00.

Jasmine: Well, how much would that be per month?

Al: That depends on the financing. It could be $200.00 a month for 5 years with no down payment. Do you have money for a down payment?

Jasmine: Uh, no. I did not realize I would need money for a down payment!

Al: Do you have a job?

Jasmine: Yes, I usually make about $200.00 a month from babysitting. I do not really have any other expenses, but I do not want to spend everything I make on a car!

Al: I have this nice red car over here. (*Al, Jasmine, and Rick walk toward another car.)* You can finance this one for $125.00 a month, and then it is yours to own after 6 years.

Jasmine: I can afford that!!

Rick: Remember, you'll need to pay for insurance, maintenance, gas, and everything else that comes along with owning a car…

Jasmine: I really want this one, Dad, and I can afford it!

Al: Step into my office and we can get this little lady her car. (*Al, Jasmine, and Rick walk into Al's office and all sit down*.) Ok, now will you be cosigning this loan for your daughter?

Rick: Yes, she's only 17, so I will be cosigning. (*Turning to his daughter.)* Now you know I expect you to pay the bill on time every month, right? I expect you to be responsible!

Jasmine: Yes, Dad, I know. I'll make sure I have the money to pay for everything…including fuzzy dice!! (*Everyone laughs*).

Narrator: *Jasmine ends up financing the car for $125.00 per month for 6 years. She does not realize that one reason the payment was lower per month was because the term of the loan was extended—meaning she will pay the loan back over a longer time period. This means that she will pay more in interest than if the term of the loan were shorter. After driving the car for 2 years, Jasmine went to start the car to go to work one morning and it made a funny noise and would not start. It ended up costing $2,000.00 in repairs! Jasmine was disappointed to find out that the $500.00 in insurance she paid every year did not cover the repair. Was financing this car the right idea for Jasmine? What should she have looked out for when shopping for a car?*

Leasing My First Car

Characters:

- Big Al, the car salesman
- Todd
- Sharon, Todd's mother
- Narrator

Narrator: *Todd and Sharon are walking around Big Al's Super Used Cars lot and Big Al approaches them as they are looking at a green truck.*

Al: Hello there, folks! How can I help you this beautiful afternoon?

Todd: I want a car!!

Sharon: (*Giving her son a stern look*.) Yes, my son is looking for a car he can purchase.

Todd: No, Mom, I want to *lease* a car. I am going to college in 2 years and I will not be able to take my car on campus. I am just looking for a car for work and to drive to school and stuff until I graduate.

Al: Sounds like you know what you want!

Todd: Yes sir. It will cost me less in the end and I do not want the long-term loan right now. I only plan on driving around town and I will return the car when the lease expires. So how much does this cool truck cost? (*Points to a nearby truck he has been looking at.)*

Al: I can lease that to you for $200.00 a month. Is that in your price range?

Todd: Wow, that's a lot more than I thought! I do not have a job right now so coming up with $200.00 a month may be difficult. What if I promise that I will get a job, Mom?

Sharon: You cannot just promise to get a job, Todd! I thought you said you had saved some money from working at the restaurant this summer?

Todd: Yeah, I have money for a down payment and the first few payments, but I will need to find a job so I can continue to make the monthly payments.

Al: Maybe you need to come back when you have a job and you know that you can afford this nice truck?

Todd: No! I want it now. I told all my friends that I would drive them to the big game next weekend! I know I can find a job in the next few weeks, and I have the money for the down payment and the first month. (*Turns to Sharon.)* Mom, can I please get this truck??

Sharon: It is your decision, but don't forget that your father and I do not want to cover the payments if you cannot make them.

Todd: I know, I know! Ok, I want to get it!!

Al: Alright, just step into my office and we will see what we can do!

Narrator*: Sharon leases the car on Todd's behalf. Sharon and Todd agree that Todd is responsible for the payment and all expenses. Todd finds a part-time job; however, he did not realize that gas would be so expensive because he is the one always driving his friends around. Every month he struggles to make the payment. He has to give up buying items like CDs and clothing just so he can make the lease payment. After 2 years, Todd turns the leased car back in to the dealership and realizes that he has paid $4,800.00 for the car, and now he has nothing to show for it! Was this the right choice for Todd? What could he have done differently?*

Financing a Car

Getting a car loan is also referred to as financing a car. A car loan can be used to purchase a new or used car. Your car becomes your collateral for the loan, which means the lender will hold the car title until the loan is paid off. The title indicates who owns the car.

If you do not pay off the loan, the bank can take back the car and then sell it to get the remaining loan amount back. New car loan terms typically are for 3 to 7 years and used car loans usually are for 2 to 5 years.

A car loan might be one of your biggest expenses. Therefore, if you decide to purchase a car, you should know exactly how much you are paying for the car and exactly how much you need to borrow.

When shopping for a car, do not negotiate or make a decision based just on the monthly payment, even if the car dealer suggests it. The total amount you will pay depends on the price of the car you negotiate, the APR, and the length of the loan.

You decide to buy a used car and have saved $2,500.00 from your summer job for a down payment. You find a car you like and the monthly payment is $225.00 for 60 months with your $2,500.00 down payment. The tax and registration fee is $575.00 and the APR is 12.10 percent.

With this information, you figure the total cost of the car to be:

$225.00	Monthly payment
x 60	Number of payments
$13,500.00	Total of payments

$13,500.00	Total of payments
$2,500.00	Down payment
+ $575.00	Tax and registration fee
$16,575.00	**Total cost of the car**

Now we can figure out how much the loan actually costs by comparing $16,575.00 to the cost of the car if you were to pay cash. If you pay cash for the car and do not take out a loan, the car dealer tells you he will give you a deal so that the car costs $12,595.00, plus tax and registration:

$12,595.00 + $575.00 = **$13,170.00**

Now that you know the cost of the car if you paid cash and the cost of a 60-month loan, you can figure out the difference which would be the cost of your loan.

$16,575.00 – $13,170.00 = **$3,405.00** (the interest for the loan)

When considering a car loan, be sure to shop around for the best deal before you make a commitment.

Repayment Terms

After you determine the size of loan you need, try to pick a repayment period that makes sense for you. For example, a $15,000.00 loan at 4 percent interest for 36 months equals a monthly payment of $443.00. Stretch the same loan out to 48 months and the monthly payment drops to $339.00. However, do not make the common mistake of thinking only in terms of monthly payments rather than the total cost of the loan. Extending a loan term will cost you more since you will be paying interest on the loan another year or more.

Be especially cautious before taking an auto loan term of 5 years or more. If you have cash for a down payment and you still have to take out a 5 to 7 year loan to afford the payments, you are likely trying to buy more car than you can really afford. You will also find that in the later years of the loan you will still be making payments on what will be an older vehicle that may have significant repair and maintenance costs. You may also still owe more on the loan than the trade-in value of the car in 5 or 7 years and that puts you in a difficult financial position.

Where to Obtain a Car Loan

You can obtain a car loan from:

- Banks/thrifts
- Credit unions
- Finance companies
- Car dealerships

Financing through Banks and Credit Unions

The financial institution where you already have an account is a good place to start when you need to finance a car. However, you should still shop around to make sure you are getting the best deal.

Most lenders can pre-approve you for a car loan. This means the financial institution calculates how much money they will lend to you to buy your car. Pre-approvals are typically a free service and you are not required to accept the loan offer from the financial institution.

Financing through a Car Dealer

Car dealers may also offer to finance your car loan.

Dealers may offer low loan rates for specific cars. To get the lowest advertised rate, you might have to:

- Make a large down payment
- Agree to a short loan term, usually 3 years or less
- Have an excellent credit history
- Pay additional fees or purchase additional products that are not necessarily reflected in the APR

Remember that a dealer offering a low interest rate is likely to be less willing to negotiate on the price of the car. Therefore, you may find that it is more affordable to negotiate a lower price on the car and finance through your own financial institution than it is to accept the dealer’s offer of a low-interest rate loan.

Activity 4: Beware of Dealer-Lender Relationships

It is important to shop around for the best financing for your car. Dealers will often try to make extra profit through the loan process. A dealer might have business relationships with many different lenders, so when you ask the dealer for financing, they might call several lenders.

Instead of picking the lender with the best rate for you, some dealers might pick the lender that makes the most profit for the dealership. For referring you and other customers, the lender might pay money to the dealership. Therefore, be aware that financing obtained by the dealer, even if the dealer contacts lenders on your behalf may not be the best deal you can get.

Instructions

- Read the scenario carefully.
- Write down some things that Sam could have done differently.
- Be prepared to explain your answers.

Scenario

Sam assumed the dealer would give him the best deal and did not shop around for a car loan. After all, he was able to negotiate the best price at this dealership: $6,000.00 for a used pickup truck.

The dealer told Sam that if he paid $1,000.00 as a down payment, he could get a car loan for 16 percent. Sam accepted the agreement without researching other possibilities.

This is what happened:

- The car dealer called several lenders in the area for Sam.
- Lender A told the dealer that Sam qualified for a $5,000.00 car loan for as low as 10 percent.
- However, Lender A had an agreement with the dealer stating that for any rate over 10 percent, the lender and the dealer would split the profit. This gives the dealer an incentive to work with Lender A and to charge Sam a high interest rate.
- In this case, the dealer quoted Sam a 16 percent rate.
- The difference between a 16 percent loan and 10 percent loan is

$921.00. That means Sam paid $921.00 more than he had to pay.

- The dealer and Lender A split the $921.00.

What could Sam have done differently?

Auto Financing Tips

Consider the following auto financing tips when purchasing a car:

- Order a copy of your credit report and correct any errors several months before shopping for a car.
- Shop around for auto financing before going to the dealer. Get pre-approved for a loan by a bank or credit union.
- Compare APRs from local banks, thrifts, credit unions, websites, and newspapers.
- Make the largest down payment you can. Beware of a low down payment or long repayment plans. The more you borrow and the longer you pay on the loan, the more interest you will pay. And if you have to sell your car in the first few years, you could owe the lender more than the car is worth.
- Consider paying for the tags, title, and taxes separately, rather than financing them. This can reduce the amount of interest you pay.
- Negotiate the best price on the car if you are going to apply for a loan at the dealership. Beware of dealers who insist on asking you how much you can afford to pay every month. These dealers might be trying to make you stretch out the term of the loan to make the loan sound more affordable. However, extending the length of the loan will increase your total cost.
- Be aware of penalties. Some lenders might charge you a *pre-payment penalty* for paying off your loan early.
- Ask whether you will get your deposit back, if required, if you change your mind. If so, get it in writing.
- Be aware that service contracts, credit insurance, extended warranties, and other options are not required and can be costly over the term of the loan. You might be given the option to buy credit insurance to pay off your loan if you should die or become disabled. Before you buy

credit insurance consider the cost, and whether it is worthwhile. Check your existing policies to avoid duplicating benefits. Credit insurance is not required by federal law.

- Be careful of ads that promise loans for people with bad credit. These deals often require a higher down payment or have a very high APR.

Car Title Loans

Title loans are short-term (usually 1 month) loans that allow you to use your car as collateral to borrow money. They may sound like a good way to get quick cash, but they can be very costly.

Activity 5: Beware of Car Title Loans

Read the scenario and answer the question.

Scenario

Michael had $500.00 in unexpected medical expenses and needed a loan. He saw a television commercial that declared, "If you have a car, you can get a loan." Michael had a car worth about $2,500.00, so he decided to apply for the loan.

The finance company Michael saw in the commercial loaned him $500.00 at 20 percent interest per month. Note that the finance company did not advertise the APR. The finance company took his car title as collateral and Michael kept the car. With a 20 percent monthly interest rate on the $500.00 loan, Michael owed $600.00 at the end of the month: the $500.00 loan plus $100.00 in interest.

Michael could not repay the $600.00 at the end of the month. The lender could have repossessed the car. However, the lender gave Michael the option of just paying the $100.00 interest and gave him until the next month to pay the loan. At the end of the next month, Michael still owed $600.00 ($500.00 loan + another $100.00 in interest) and still could not repay. By the end of one year, Michael had paid $1,200.00 ($100.00 x 12) in interest for his $500.00 loan. This equates to a loan with a 240 percent APR. Finally, Michael received a bonus from work and was able to pay off the $600.00.

This is an expensive way to borrow money! What could Michael have done differently?

How to Pay for College

It is well documented that getting an education will lead you to a path of economic success. Those who complete educational programs after high school, on average, enjoy more job opportunities and earn better salaries than those with less education. Pursuing a college degree can be both time consuming and expensive. However, college graduates usually see a return on their investment and benefit from long-term payoffs (e.g., more career options, better promotion opportunities, higher earnings, and lower unemployment on average). For instance, data collected by the Census Bureau in 2008 shows that bachelor's degree recipients earned on average about $26,000.00 more than workers with a high school diploma.

Continuing your education beyond high school is a large investment that will need a lot of planning and research. If you are planning to go to a college or university; community college; trade, career, or technical school; or are entering the workforce it is never too late to think about how you will pay for your expenses.

Financial Aid Overview

Federal Student Aid (FSA) provides more than 150 billion dollars annually to help over 14 million students go to college. Federal student aid programs include the Pell grant, student loans, and college work-study programs. Completing the Free Application for Federal Student Aid (FAFSA℠) is the first step you need to take to apply for federal student aid. In addition, most states and schools use FAFSA information to award their financial aid.

Tips to Getting Aid

Financial aid administrators and guidance counselors agree that the following tips speed up the aid application process:

- **Apply Early**
  Applying early can increase your chances for receiving nonfederal student aid. State and school deadlines will vary and tend to be early. Check with them to find out their exact deadline dates so you can submit your FAFSA on or before this date.

- **Read the Instructions**
  Many questions on the FAFSA are straightforward (e.g., what is your Social Security number?). However, if you do not understand a questions or the information required, there are tools available (e.g., online chat and help text) to assist you if you questions. You can read and complete the questions before entering your information online by downloading the FAFSA on the Web Worksheet at www.fafsa.ed.gov/before012.htm.
- **File Electronically**
  Complete and submit your FAFSA online. It is the fastest and most accurate way to apply for student aid.
- **Complete Your Tax Return**
  It is recommended that you (and your parents if you are a dependent) complete your tax return, if applicable, before filling out your FAFSA. This will make completing the FAFSA easier because tax information is required. You can estimate your tax information on the FAFSA until your tax return has been completed. After that, you must update your FAFSA online or provide your school with actual tax return information.
- **Additional Forms**
  Many schools and states rely on the FAFSA as the single application for student aid. However, your school or state may require additional forms. Check with your state agency and the financial aid office at the school you plan to attend to find out if they require additional forms.

How is the FAFSA used?
The information from your FAFSA is used to calculate your Expected Family Contribution (EFC). The EFC is an index schools use to estimate how much financial aid (grants, loans, or work-study money) you would receive if you were to attend their school.

Federal Student Aid Programs
The U.S. Department of Education offers three major types of federal student aid:

- Grants (gift aid)

- Campus-based aid, which is a combination of work, grant, and loan funds
- Loans, which must be repaid with interest

Scholarships

A scholarship is money for college that you will not be expected to repay. Scholarships are definitely worth seeking! Scholarships sponsored by colleges are often designated for students who fit a particular profile (i.e., students who are from the college's home state, hold a specified grade point average, enroll in a particular major, or bring special talent (e.g., in athletics or in music)). You will need to check with each college to see what scholarships are available.

Other outside scholarships may be available to students whose parents work for a particular company or to students who are eligible for scholarships sponsored by religious or civic organizations. At the same time, though, be very wary of companies that guarantee or promise you scholarships, grants, or fantastic financial aid packages in exchange for a fee. Many of these are scams, and you will simply lose your money and risk giving your personal information to a potentially unscrupulous business or individual. You can learn more about avoiding scams by visiting the FTC's website: *http://www.ftc.gov/bcp/menus/consumer/education/scholarships.shtm*.

Potential Grant Programs

Grants, like scholarships, do not have to be repaid and are offered to a variety of students. Let us look at some different grant programs.

Federal Pell Grant

Federal Pell Grants are usually awarded to undergraduate students who have not earned a bachelor's or a professional degree. Pell Grants are considered a foundation of federal financial aid, to which aid from other federal and nonfederal sources might be added.

How much can I get?

The maximum Pell Grant award changes each award year depending on program funding (e.g., the maximum award for the 2010–2011 award year is

$5,500.00). A student attending college year-round (e.g., during summer, fall, and spring terms) could receive as much as two maximum awards in a row during that time period. The amount you receive depends not only on your financial need, but also on your costs to attend school, your status as a full-time or part-time student, and your plans to attend school for a full academic year or less.

If I am eligible, how will I get the Pell Grant money?
Your school can apply Pell Grant funds to your school costs, pay you directly (usually by check), or combine these methods. The school must tell you in writing how much your award will be and how and when you will be paid.

Federal Supplemental Educational Opportunity Grant
The Federal Supplemental Educational Opportunity Grant (FSEOG) program is for undergraduates with exceptional financial need. Pell Grant recipients with the lowest Expected Family Contributions (EFCs) will be considered first for a FSEOG.

How much can I get?
You can receive between $100.00 and $4,000.00 a year, depending on when you apply, your financial need, the funding at the school you are attending, and the policies of the financial aid office at your school.

If I am eligible, how will I get the FSEOG money?
If you are eligible, your school will credit your account, pay you directly (usually by check), or combine these methods.

Teacher Education Assistance for College and Higher Education Grant
The Teacher Education Assistance for College and Higher Education Grant (TEACH Grant) is for students who intend to teach in a public or private elementary or secondary school that serves students from low-income families. You must be enrolled as an undergraduate, post baccalaureate, or a graduate student in a school that participates in the TEACH Grant program and meet certain academic achievements and course requirements to receive a TEACH Grant. Additional conditions may apply.

How much can I get?

You can receive up to $4,000.00 per year.

If I am eligible, how will I get the TEACH Grant money?

Before receiving TEACH Grant money, you must sign an "Agreement to Serve." This agreement specifies:

- The conditions under which the grant will be awarded
- The teaching service requirements
- Your acknowledgment that if you do not meet the teaching service requirements you must repay the grant as a Federal Direct Unsubsidized Loan, with interest accrued from the date the grant funds were disbursed

A TEACH Grant Fact Sheet is available online at: *http://studentaid.ed.gov/PORTALSWebApp/students/english/TEACH.jsp*.

Iraq and Afghanistan Service Grant

Students who are not eligible for a Pell Grant may be eligible for the Iraq and Afghanistan Service Grant if:

- A parent or guardian was a member of the U.S. Armed Forces and died as a result of service performed in Iraq or Afghanistan after September 11, 2001
- You are under the age of 24, and
- You were enrolled in college (at least part-time) at the time of the parent or guardian's death

How much can I get?

The grant award is equal to the amount of a maximum Pell Grant for the award year, and the payment is adjusted if you are enrolled less than full time.

If I am eligible, how will I get the Iraq and Afghanistan Service money?

If you are eligible, your school will credit your account, pay you directly (usually by check), or combine these methods. The school must tell you in writing how much your award will be and how and when you will be paid.

Institutional Grants

Colleges provide institutional grants to help make up the difference between college costs and what a family can be expected to contribute through income, savings, loans, and student earnings.

Other institutional grants, known as merit awards or merit scholarships, are awarded on the basis of academic achievement. Some merit awards are offered only to students whose families demonstrate financial need; others are awarded without regard to a family's finances.

Some grants come with special privileges or obligations. You will want to find out about the types of grants awarded by each college you are considering.

Federal Loan Programs

If grants and scholarships are not enough to pay for college, you can look into federal loan programs. If you think you need a loan do your homework, ask questions, and compare loans before settling on one. Your state's department of education and the college's financial aid department are good resources when deciding on which type of loan is best for you.

Getting A Federal Student Loan

Like other federal student aid programs, the information from your FAFSA is used to determine the types and amounts of federal student loans you can receive. This means that you first must complete the FAFSA before receiving a federal loan.

Federal loans include:

- Federal Perkins Loans
- Direct Stafford Loans (Direct Loans^{SM})

Federal Perkins Loan

A Federal Perkins Loan, or Perkins Loan, is a low-interest (5 percent) loan for students with exceptional financial need. If your school participates in the Federal Perkins Loan program, the loan will be made through the school's financial aid office and your school or the school's loan servicer will inform you about your loan eligibility.

Your school is your lender, and the loan is made with government funds. You will have to sign a promissory note (a legally binding document) that lists the conditions under which you are borrowing and the terms under which you agree to repay your loan.

How much can I borrow?
You can borrow up to $5,500.00 for each year of undergraduate study (the total you can borrow as an undergraduate is $27,500.00). For graduate studies, you can borrow up to $8,000.00 per year (the total you can borrow as a graduate is $60,000.00, which includes amounts borrowed as an undergraduate). The amount you receive depends on when you apply for the loan, your financial need, and the funding level at the school. Your school will either pay you directly (usually by check) or apply your loan to your school charges.

Other than interest, is there a charge for this loan?
No, there are no other charges. However, if you skip a payment, if your payment is late, or if you make less than a full payment, you might have to pay a late charge and collection costs.

Direct Stafford Loans (Direct Loans℠)
Direct Loans, from the William D. Ford Federal Direct Loan (Direct Loan) program, are low-interest loans for eligible students to borrow directly from the U.S. Department of Education at participating schools. There are several types of Direct Loans:

- **Direct Subsidized Loans:** You are not charged interest while you are in school (at least half-time) and during grace periods and deferment periods.
- **Direct Unsubsidized Loans:** Interest is charged and accumulates on an unsubsidized loan from the time it is first paid out. You have the option to pay the interest on your unsubsidized loan while you are in school.
- **Direct PLUS Loans:** These loans are for parents of dependent students and graduate and professional degree students. Interest is

charged during all periods, beginning on the date the loan is first disbursed.

- **Direct Consolidation Loans:** These loans combine federal education loan debts into a single loan.

How much can I borrow?
The maximum amount you can borrow ranges from $5,500.00 per year for a dependent freshman to $20,000.00 per year for a graduate or professional degree student. However, the actual amount you are eligible to receive each year is determined by your school and may be less than the maximum amount. There are also limits on the total amount of your loan debt.

Direct PLUS borrowers have no set limits, but cannot borrow more than the total education expenses minus any other financial aid received (e.g., a Direct Subsidized or Unsubsidized Loan). The school will determine the actual amount a parent or graduate/professional degree student can borrow.

Other than interest, is there a charge for this loan?
Yes. In addition to interest, you pay a loan fee that is a percentage of the principal amount of the loan. The fee is deducted before you receive any loan money, so the loan amount you actually receive will be less than the amount you have to repay.

Repaying Your Federal Loan
After you graduate, leave school, or drop below half-time enrollment you have a period of time before you must begin repayment. This period of time is called the "grace period." Your loan servicer will notify you when you have to start making loan payments.
The "grace period" for each loan type will generally be:

- Nine months for Federal Perkins Loans
- Six months for a Federal Direct Stafford Loan
- There is no grace period for a Direct PLUS Loan. Repayment begins 60 days after the loan money is fully disbursed. In some cases, PLUS borrowers may be able to postpone repayment with the loan servicer.

It is very important to make your full loan payment according to your repayment schedule. If you do not, you could end up in default, which has serious consequences (e.g., your credit report will be damaged and the ability to obtain new credit or even qualify for certain jobs may be jeopardized). Student loans are real loans—just as real as car loans or mortgages—and you have to pay them back.

Therefore, do not borrow more than you need for school-related expenses that are not covered by grants, scholarships or other sources. Tell your student finance aid office if you do not need to borrow all the money that you are eligible to borrow. The less money you borrow, the less you will have to pay in interest—and you will be able to enjoy more of your income once you graduate without having to worry about paying back as much debt!

Managing Your Student Loan Payments

You will have several types of repayment plans to choose from to help you manage your federal student loans. You can also explore other options to manage your student loan payments after graduation (e.g., loan consolidation). Be sure to fully research the pros and cons of consolidation before signing any paperwork. Student loan consolidation can be used to:

- Reduce your monthly student loan payment. However, like a car loan, extending the years of repayment increases the total amount you have to repay.
- Simplify your finances by making one payment per month.

The U.S. Department of Education's National Student Loan Data System (NSLDS℠) provides information on any federal loans you receive. However, NSLDS does not include information on any private loans you may receive. You can access NSLDS at www.nslds.ed.gov.

Nonfederal loans

There are also private, nonfederal loans available to you. A private student loan is issued by a lender (e.g., a bank or credit union). Private student loans differ from federal loans in that they often have higher interest rates and loan fees, usually require a credit check, and do not provide the benefits of federal student loans.

Federal student loans also offer borrowers many benefits not typically found in private loans, including:

- Low fixed interest rates
- Cancellations for certain employment
- Deferment (postponement) options

For these reasons, you and your parents should always exhaust federal student loan options before considering a private loan.

You should also fully understand the pros and cons of any loan product.

Activity 6: Ways to Pay for College

Now that you have learned about several ways to pay for college, read each scenario and determine whether each student may be eligible for a scholarship, grant, and/or federal student loan.

Scenario 1

Grace wants to go to a fashion design school when she graduates from high school. She has checked out a school near where she lives, and there are a few schools that offer programs online. These options would save on room and board costs, but she would still need to determine how she could pay the tuition. She makes average grades and her parents have a moderate income.

Scenario 2

Todd comes from a low-income family, so he knows his parents will not be able to help him with college costs. He has been trying to work and save for school. He does well in school and has a fairly high grade point average.

Scenario 3

Ramón’s parents are from Peru, but Ramón was born in the U.S. and dreams of going to college (preferably in-state) and working for NASA. He is not sure how he is going to pay for college, but he has a 4.0 grade point average and he is one of the top soccer players at his school and in his district.

Federal Work-Study

The Federal Work-Study (FWS) program provides part-time jobs for undergraduate and graduate students who need financial assistance to help pay for education expenses. The program encourages community service work and work related to the recipient's course of study.

Will I be paid the same as I would in any other job?

You will be paid by the hour if you are an undergraduate. No FWS student may be paid by commission or fee. Your school must pay you directly (unless you direct otherwise) and at least monthly. Wages for the program must equal at least the current federal minimum wage. The wages may be higher depending on the type of work you do and the skills required. The amount you earn cannot exceed your total FWS award. When assigning work hours, your employer or financial aid administrator will consider your award amount, your class schedule, and your academic progress.

What kinds of FWS jobs are there?

You will usually work for your school. If you work off campus, your employer will usually be a private nonprofit organization or a public agency and the work performed must be in the public interest.

Your school may also have agreements with private for-profit employers. This type of work-study must be relevant to your course of study (to the maximum extent possible). If you attend a career school, there might be further restrictions on the jobs you can be assigned.

Other Ways to Help Offset the Costs of College

What are other ways to pay for college or keep college costs down?

Calculate College Costs

When deciding on how to pay for college, tuition is not the only thing you will need to consider. There are many other costs (e.g., books, fees, and housing) that add up to a significant amount of money.

The cost of the college should be considered along with the academic programs of a school. College comparison shopping should include options (e.g., comparing 2-year community colleges and schools close to home with other 4-year colleges) that can help save on room and board.

The Cost of College Calculator

The Cost of College Calculator will help you determine your expenses and estimate your total available income for college. You will need to consider all of your resources and the total cost of your education.

Even if you do not plan on attending college, this worksheet will give you an idea about the costs you will have after high school whether you are moving to your own apartment, buying a car, or taking other steps for completing your education beyond high school. Take a moment to review the worksheet. Is there anything that surprises you? What other things might you include that are not listed on the worksheet?

You can complete the worksheet after class. Some of the categories are broken down so that you can estimate the total cost. When you have finished entering your estimates, add together all of the numbers in the Expense column and all of the numbers in the Income column. Then subtract the expenses from the income to determine whether you have enough income to cover the expenses.

Cost of College Calculator

Expenses		Income	
Education	$	Family Contribution	$
Tuition		Parents	
Books		You	
Fees		Friends/Relatives	
Supplies			
Transportation	$	Financial Assistance	$
Bus/Air/Train		Summer Job Savings	
Car Payment		Other Savings	
Car Repair/Insurance			
Fuel Costs			
Housing	$	Financial Aid Grants	$
Mortgage		Pell	
Dormitory/Rent		FSEOG	
Utilities		Iraq & Afghanistan Service Grant	
		Teacher Education Assistance for College	
Telephone		Institutional	
		State	
Food	$	Federal Loans	$
Room & Board Plan		Federal Perkins	
		Direct Stafford (Subsidized)	
Groceries		Direct Stafford (Unsubsidized)	
		Direct PLUS (parents and graduate or professional students)	
Health	$	Other Loans	$
Insurance		Other	
Doctor/Prescriptions		State	
Personal/Miscellaneous	$	Employment	$
Laundry/Cleaning		Federal Work-Study	
Drug Store Items		Institutional	
Clothing		Off-Campus	

Entertainment	$	Scholarships	$
In-School Interest	$	Other Income/Resources	$
Direct Unsubsidized Loan			
Emergencies	$		
Other Expenses	$		
Credit Card Payment			
Total Expenses	$	**Total Income**	$

Income – Expenses = $______________ Your Balance

Module Summary

Congratulations! You have completed the *Paying for College and Cars* module. We have covered a lot of information today about financing two big goals. You learned about:

- Secured and unsecured loans
- The Four Cs of loan decisions
- Car loans and auto financing
- Some of the ways to finance a college education

You now know what to consider when shopping for these loans.

Knowledge Check

1. What is an unsecured loan?
    a. A loan where the borrower offers collateral for the loan
    b. A loan where no collateral is needed
    c. A low interest-rate loan
    d. A loan that can be approved quickly

2. Who holds the car title (or owns the car) while you are making loan payments?
    a. You
    b. A parent or guardian who cosigns the loan
    c. The lender
    d. The car dealership

3. Select all that apply. If you lease a car, you may pay extra for:
    a. Wear and tear
    b. Insurance
    c. Mileage
    d. All of the above

4. What are some ways to help reduce the costs of education after high school?
    a. Choose a tuition-free school or one with lower tuition costs
    b. Apply for student loans
    c. Apply for grants, scholarships, or work-study programs
    d. All of the above

5. What are the benefits of an unsecured installment loan? Select all that apply.
    a. Fast approval times
    b. Lower interest rates than secured loans
    c. Lower interest rates than other types of unsecured loans (e.g., credit cards)
    d. More lenient credit requirements than secured loans

6. Which of the following is an example of a secured installment loan?
    a. Auto loan
    b. Education loan
    c. Credit card
    d. Medical expenses

7. ________ is the cost of borrowing money on a yearly basis?
    a. APR
    b. Finance charge
    c. Collateral
    d. Interest

8. Which of the following Four Cs refers to your present and future ability to meet your payment obligations?
    a. Capacity
    b. Capital
    c. Character
    d. Collateral

9. What can you do to get the best car loan rate for you and pay less interest? Select all that apply.
    a. Make a large down payment
    b. Agree to a longer term loan (e.g., 5 years or more)
    c. Shop for the best rates
    d. Pay additional fees or purchase additional products to lower the rates

10. Before signing any loan paperwork, you should:
    a. Make sure you can afford the monthly payment
    b. Read the agreement and ask questions
    c. Look for hidden fees and charges
    d. All of the above

11. You are not required to pay back which of the following? Select all that apply.
    a. Scholarships
    b. Grants
    c. Federal student loans
    d. Work-study earnings

12. Which of the following might you receive if you are in exceptional financial need?
    a. Federal Perkins Loan
    b. TEACH Grant
    c. Federal Supplemental Educational Opportunity Grant (FSEOG)
    d. Nonfederal loan

13. What is Expected Family Contribution?
    a. How much money you and your family plan to contribute toward your education
    b. An estimation of your (or your parent's) income to be used for upcoming tax returns
    c. The time prior to when you need to make repayments on your loan
    d. An index used to estimate how much financial aid you will receive

14. What is collateral?
    a. A loan that is repaid in equal monthly payments or installments for a specific period
    b. Security (or an asset) you promise to a lender if you do not pay back the loan
    c. The dollar amount the loan will cost, including: interest, service charges, and loan fees
    d. The value of your assets and your net worth

Glossary

Annual Percentage Rate (APR): A measure of the cost of your loan expressed as a yearly percentage rate.

Capacity: One of the Four Cs of loan decision-making; capacity is your present and future ability to meet your payment obligations.

Capital: One of the Four Cs of loan decision-making; capital refers to the value of your assets and your net worth.

Car Lease: An agreement between you and the car dealer, manufacturer, or other company that allows you to essentially rent the car for a period of time.

Car Title: A legal document that indicates who owns the car.

Character: One of the Four Cs of loan decision-making; character refers to how you have paid bills or debts in the past.

Collateral: One of the Four Cs of loan-decision making; collateral is a piece of property or an asset that you promise to give to the bank if you cannot pay back the loan.

Default: Failure to repay a loan according to the terms agreed to when you signed your promissory note.

Deferment: A temporary suspension of a borrower's monthly loan payment.

Disbursement: Payment of loan money made to you.

Equity: The value of your home (or other asset) minus the debt.

Expected Family Contribution (EFC): A number used by your school to determine your eligibility for federal student financial aid.

FAFSA (Free Application for Federal Student Aid): An application for federal student financial aid (e.g., Pell grants, student loans, and college work-study programs).

Finance Charge: The dollar amount (including interest, service charges, and loan fees) the loan will cost you.

Fixed-Rate Loan: A loan with an interest rate that stays the same throughout the term of the loan.

Grace Period: The time between when you graduate, leave school, or drop below half-time enrollment and when you must make payments on your student loan.

Grants: Money given to you for college that you will not be expected to repay.

Installment Loan: A loan that is repaid in equal monthly payments, or installments, for a specific period of time, usually several years.

Loan Pre-Approval: Loan pre-approval occurs when a financial institution calculates how much money you can borrow.

Loan Servicer: An entity designated to track and collect a loan.

Participation Fee: Money that some dealers and finance companies might charge you to get a low interest rate.

Principal Amount: The amount of money borrowed. Interest is charged on this amount.

Scholarship: Money for college that you will not be expected to repay. Scholarships sponsored by colleges are often designated for students who satisfy certain criteria or other factors.

Secured Loan: A loan secured guaranteed by collateral.

Title Loan: A short-term (usually 1 month) loan that allows you to use your car as collateral to obtain money.

Unsecured Loan: A loan that is not secured by collateral.

Variable-Rate Loan: A loan with an interest rate that might change during the period of the loan.

For Further Information

Federal Deposit Insurance Corporation (FDIC)

www.fdic.gov/consumer

1-877-ASK-FDIC (275-3342)

Visit the FDIC's website for additional information and resources on consumer issues. For example, every issue of the quarterly *FDIC Consumer News* provides practical hints and guidance on how to become a smarter, safer user of financial services. Also, the FDIC's Consumer Response Center is responsible for:

- Investigating all types of consumer complaints about FDIC-supervised institutions
- Responding to consumer inquiries about consumer laws and regulations and banking practices

U.S. Financial Literacy and Education Commission

www.mymoney.gov

1-888-My-Money (696-6639)

MyMoney.gov is the U.S. Government's website dedicated to teaching all Americans about financial education. Whether you are planning to buy a home, balance your checkbook, or invest in your 401k the resources on MyMoney.gov can help you. Throughout the site you will find important information from federal agencies.

Federal Consumer Information Center

www.pueblo.gsa.gov

1-800-688-9889

The Federal Consumer Information Center (FCIC) provides free online consumer information to help the public. The FCIC produces the Consumer Action Handbook, which is designed to help citizens find the best sources for assistance with their consumer problems and questions.

Federal Trade Commission

www.ftc.gov/credit / 1-877-FTC-HELP (382-4357)

The Federal Trade Commission (FTC) website offers practical information on a variety of consumer topics, including privacy, credit, and identity theft. The FTC also provides guidance and information on how to select a credit counselor.

Department of Education

www.ed.gov/participants/

The Department of Education provides Information relating to college, financing, and student aid.

For other education-related resources:

- Complete the FAFSA online at www.fafsa.ed.gov/
- Find out more about scholarships at www.ftc.gov/bcp/menus/consumer/education/scholarships.shtm
- For more information on federal loan programs, visit http://studentaid.ed.gov