

Parent Handbook: How Interest Works

If you or your student use loans to help pay for college, you will need to pay some form of interest on the loans. Simply put, interest is the cost you pay to borrow the money.

Interest is included in all student loan types, whether it's federal loans or private loans you may take out to help your student. And that interest can add up and increases the total amount you need to pay back.

But the total amount that will need to be paid back depends on several factors, including the amount you borrow, the interest rate and the repayment terms.

For example, if you borrow \$10,000 dollars at a fixed 6% interest rate, a 0% origination fee and pay the loan off with regular monthly payments over a 10-year period, you will end up paying approximately a total of \$13,330 dollars by the end of the loan.

And the more you borrow and the higher the interest rate the more you will pay back in total over the life of the loan. To better understand your payment obligations, here are some key items to know whenever you or a student takes out a student loan.

The disbursement date, which is the date the funds arrive and usually when interest starts accruing. There are exceptions, like subsidized federal loans for your student where the government pays the interest while your student is in school full time.

The total amount borrowed in each loan.

The interest rate on each loan and whether those rates are fixed for the life of the loan, or variable, which means they can change. How the interest accrues, which is typically calculated daily for student loans. Interest on student loans accrues through a simple interest calculation.

When your first payment is due; this can vary as there are different repayment options depending on the type of student loan taken out. And your payment schedule, so you know how long you will be making payments if you are just making the minimum monthly payment.

It's vital to understand not just what your interest rate on a student loan is, but all of your repayment terms so you can stay on track to repaying the loan and perhaps find ways to pay extra to help cut back on the total interest you end up paying.

No matter what pops up along the way, you'll be prepared for your college financing journey.

Learn other helpful college financing tips in the Parent Handbook.