Five Payment Options for College

Option #1 –Current Savings & Investments

Today, this is the best option. But in most cases unrealistic for many families. However, if you can afford to write one large check to cover the remaining balance through current savings and cash flow, please do so. There might be a future time when the college loan rates are less than investment rates, and this strategy might not be as beneficial. With high loan rates on the horizon and investment rates still low, paying for college using cash flow and savings is best if you can afford it.

The only downside of using your savings and investments to pay your child's college is that you are taking most of the financial risk if your child does not graduate from college. You are prepaying college with the hope they will graduate. Unfortunately, you are reducing your child's accountability or responsibility. Moreover, with graduation rates hovering around 37% for a four year degree in the United States and more students leaving college before they earn their degree, using current savings and investments can be very risky.

Option #2 – College Monthly Tuition Payment Plans: Cash Flow

Most colleges allow parents to make monthly payments to cover the remaining balance (True Budget). Essentially, colleges will divide your remaining balance equally using an installment plan lasting twelve months or less. Many colleges do not charge interest while you pay your balance using this short-term installment plan. The colleges basically deduct your payment amount from your checking or savings account each month. A few colleges also allow you to charge this on a credit card. However, many installment plans do have an enrollment fee (less than $100). For example, let's use a figure of $18,323 as our unmet aid or remaining balance. A college may allow us to pay this amount over 12 months or $1527 per month. The payments depend on what, if anything, you put down and when. Make sure you ask about all cost and fees before starting a tuition installment plan. The installment plan is a good alternative to paying for college if you cannot afford a large lump sum payment at the start of the semester, but you have the cash flow to cover the monthly payments.

Again, the only downside to using your cash flow to pay for college is the potential risk of using your hard earned money on a risky investment like finishing college. I know what you are thinking: "Not my child. She/he will graduate." Believe me, I have met many students that were bright, smart, intelligent, and motivated when they entered college, but never graduated. There is nothing more devastating to a family than paying for college and a child not graduating.

Option #3 – College Loans

There are many different types of loans available for you to consider. This article would be too long and too boring for me to share with you all the loans that are available and the pros and cons of each loan. For my clients, we produce a Loan Booklet that goes into detail about all your loan options and the best providers.

I will offer you a quick recommendation. Please start by taking the Federal Stafford Loans. You will need to sign the master promissory note and complete loan counseling online at www.studentloans.gov. Also, a good resource for you to compare private student loans is www.simpletuition.com. Be careful and know what you are taking before you sign on the dotted line and remember that educational loans can never be discharged through bankruptcy!

Option #4 – Home Loan: Equity or Lines of Credit

With low interest rates compared to other college loans and a potential tax deduction, using an equity line of credit or home loan has become very popular. Moreover, if your college requires you to complete the CSS Profile form or their own institutional form and home equity is used to calculate your Expected Family Contribution (EFC) number, then borrowing money from your home might be a great idea! Colleges that just use the FAFSA form do not use home equity (primary residence only) in their EFC calculation. By taking equity out of your house, you could qualify for some financial aid from the college next year because you are decreasing your assets in the expected family contribution calculation.

There is always another side of the coin with any option. For many, home equity is a source for emergency funds that can be used in times of need. Many small business owners also use their home equity to cover month-to-month cash flow fluctuations. If you tap your equity to pay for college, this source of emergency funding is no longer an option. In addition, since the home mortgage crisis began in 2008, home values have dropped and fair market values of homes have changed dramatically.

Option #5 – Downsize Your Life Style

I am not a frugal person, but I do believe in value. I want my life to be better next year and I am not one to preach “live below your means.” Sometimes making minor changes to your life can have a huge impact. For example, a pack of cigarettes can cost anywhere from $5.00 to $11.00 depending on where you live. If we use $6.50 as an average cost of a cigarette pack and you smoke a pack a day, this equals to $45.50 per week. That equals to $2366 per year that could be used toward college. Moreover, let’s say you spend $5 per day on one of these miscellaneous items: coffee, energy drinks, lunch, snack, lottery tickets, candy, etc…If you could cut this $5.00 item out of your daily routine, you could save $1820 in college cost. How about going on a “staycation” instead of a vacation this year? The average person spends around $2,200 per year on a vacation and that does not include lost wages. In this example, just a few changes added up to $6,386 that could be used toward college. Do this for four years and you have $25,544!