

---

**Office of the Comptroller of the Currency  
Board of Governors of the Federal Reserve System  
Federal Deposit Insurance Corporation  
National Credit Union Administration  
Consumer Financial Protection Bureau  
State Liaison Committee**

---

January 29, 2015

## **Guidance on Private Student Loans With Graduated Repayment Terms at Origination**

### **Purpose**

The agencies,<sup>1</sup> in conjunction with the State Liaison Committee (SLC) of the Federal Financial Institutions Examination Council, are issuing<sup>2</sup> this guidance to provide financial institutions with principles applicable to private student loans that have graduated repayment terms. Financial institutions that originate private student loans may offer borrowers graduated repayment terms in addition to fixed amortizing terms at the time of loan origination. Graduated repayment terms are structured to provide for lower initial monthly payments that gradually increase.

Although most student loan agreements include a grace period<sup>3</sup> to help with the post-education transition, the agencies and SLC recognize that students leaving higher education programs may prefer more flexibility to transition into the labor market because of a number of factors, such as competitive job markets, traditionally low entry-level salaries, and higher student debt loads. Graduated repayment terms may align borrowers' income levels with loan repayment requirements, provide flexibility to repay the debt sooner if borrowers' incomes increase more quickly than projected, and may help long-term probability of full repayment.

Graduated repayment terms are available under certain federal student loan programs. The credit risk associated with federal student loans, however, differs from that of private student loans, which are not guaranteed or originated by the federal government. Accordingly, some extended repayment features offered under the federal student loan programs may not always be appropriate for private student loans.

Financial institutions that originate private student loans with graduated repayment terms should prudently underwrite the loans in a manner consistent with safe and sound lending practices. Financial institutions should provide disclosures that clearly communicate the timing and the amount of payments to facilitate a borrower's understanding of the loan's terms and features.

---

<sup>1</sup> The agencies consist of the Board of Governors of the Federal Reserve System, the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency.

<sup>2</sup> In implementing this guidance, the agencies will examine financial institutions consistent with their respective authorities.

<sup>3</sup> A grace period is the allotted amount of time during which borrowers are not expected to make payments on student loans after initially leaving higher education programs or dropping below half-time enrollment status.

## Principles for Private Student Loans with Graduated Repayment Terms at Origination

Financial institutions should consider the following principles in their policies and procedures for underwriting private student loans with graduated repayment terms at origination:<sup>4</sup>

- **Ensure orderly repayment.** Private student loans should have defined repayment periods and promote orderly repayment over the life of the loans. Graduated repayment terms should ensure timely loan repayment and be appropriately calibrated according to reasonable industry and market standards based on the amount of debt outstanding. Graduated repayment terms should avoid negative amortization or balloon payments.
- **Avoid payment shock.**<sup>5</sup> Graduated repayment terms should result in monthly payments that a borrower can meet in a sustained manner over the life of the loan. Graduated increases in a borrower's monthly payment should begin early in the repayment period and phase in the amortization of the principal balance to limit payment shock to the borrower.
- **Align payment terms with a borrower's income.** Graduated repayment terms should be based on reasonable assumptions about the ability to repay of the borrower and cosigner, if any. Lender underwriting should include an assessment of a borrower's (and, if applicable, a cosigner's) ability to repay the highest amortizing payment over the term of the loan. Graduated repayment terms should not be structured in a way that could mask delinquencies or defer losses.
- **Provide borrowers with clear disclosures.** Financial institutions that offer private student loans with graduated repayment terms should provide borrowers with disclosures in compliance with all applicable laws and regulations. For example, the Truth in Lending Act, as implemented by Regulation Z, includes specific private student loan disclosure content requirements.<sup>6</sup> Ensuring that disclosures clearly communicate the timing and the amount of payments facilitates borrowers' understanding of their loans' terms and features.
- **Comply with all applicable federal and state consumer laws and regulations and reporting standards.**<sup>7</sup> Private student loans with graduated repayment terms must comply with all applicable consumer protection laws. These include, but are not limited to, the

---

<sup>4</sup> In addition to offering graduated repayment terms at origination, financial institutions may also offer graduated repayment terms as well as other types of workout options to borrowers experiencing financial difficulties, as addressed in "Banking Agencies Encourage Financial Institutions to Work With Student Loan Borrowers Experiencing Financial Difficulties," issued July 25, 2013 at <https://www.fdic.gov/news/news/press/2013/pr13065.html> and <https://www.fdic.gov/news/news/financial/2013/fil13035.html>.

<sup>5</sup> Payment shock occurs when a borrower experiences a significant increase in the amount of the monthly payment after a reset date.

<sup>6</sup> 12 CFR 1026.46 and 12 CFR 1026.47.

<sup>7</sup> Reporting standards include, but are not limited to, quarterly Consolidated Reports of Condition and Income.

Electronic Fund Transfer Act, the Equal Credit Opportunity Act, federal and state prohibitions against unfair, deceptive, or abusive acts or practices (such as section 5 of the Federal Trade Commission Act and sections 1031 and 1036 of the Dodd–Frank Wall Street Reform and Consumer Protection Act), the Truth in Lending Act, and the regulations issued pursuant to those laws.

- **Contact borrowers before reset dates.** Before originating private students loans with graduated repayment terms, financial institutions should develop processes for contacting borrowers before the start of the repayment period and before each payment reset date. These contacts can help establish student debt as a priority in borrowers’ payment hierarchies<sup>8</sup> and aid borrowers in responding effectively to payment increases and other potential repayment challenges.

---

<sup>8</sup> Payment hierarchy refers to the prioritization of a borrower’s payment obligations.