LifeSmarts U Personal Finance Lesson
Financial Aid—Funding Post-Secondary Education

Promissory Note Scenarios: Key and Discussion Prompts

Directions
Use the sample Promissory Note and the content vocabulary as the basis for answering these questions about the following scenarios. Be specific with each response. Explain your answers, but do not copy the language of the note. Use your own words to "decode" the contract language.

1. Rihanna has applied for a loan to finish her music degree. A credit check is ordered before her loan application is approved. Why is this done? What is her lender looking for? Content vocabulary: credit check, credit worthy Credit reporting agencies provide credit checks to potential lenders to help evaluate a loan application. This report shows the lender if you are credit worthy-outlining how past debts have been repaid.
Discussion: At eighteen, do most high school seniors have a credit history? Would they know where and how to check for it?
2. Paul has a $15,000 loan for his first year at State University. The promissory note states, "The interest on the loan will be capitalized." What does this mean? How will this affect the total amount paid? Content vocabulary: capitalization Capitalization is the process of adding unpaid interest to the principal balance of a loan. This increases the amount of interest charged since it increases the balance. It also increases the total cost of the loan.
Discussion: When an undergraduate loan is repaid over 180 months (15 years), this can be a significant charge. Do you think most high school students are aware of this and understand the consequences of committing to making payments through their 20s and well into their 30s? Explain your answer.
3. Selena, with the help of her parents, received a private loan. Unfortunately, she was seriously injured in a car accident and is unable to return to school to finish her degree. What happens to her school loan? Who is obligated to pay? Content vocabulary: cosigner, grace period Because the loan has a six month grace period, no payment is due until that time expires. Then Selena must begin to repay. Her parents are cosigners for the loan, and they are obligated to pay if she cannot.

4. Bruno notices that a few months after receiving his school loan, robocalls and messages to his cellphone have increased. What could be the possible cause? What could he do to reduce the frequency of these contacts? Content vocabulary: privacy The lender states that they may share personal and financial information with others and that they may contact you using an automatic dialer or a pre-recorded message. Bruno can cancel his consent by written notice to the address provided in the promissory note.
Discussion: Many Americans are annoyed by telemarketing and text marketing yet have not reviewed the "opt-out" directions in a contract or on a website. Why?
5. Taylor's loan has been disbursed and she is looking for the loan check in the mail. What is the most probable reason she has not received it? Where did it go? What is the COA? Content vocabulary: disbursement, COA The lenders most often disburse a loan to the school, and it is applied to the student's account. The COA, cost of attendance, is the expenses that can be paid for by the loan. If the loan, together with other financial aid, is more than the cost of attendance, the school will give the lender a partial refund of the loan.
6. Elvis's loan papers included a clause about deferment and a grace period. What is the connection between these two clauses of the contract? How do they impact his repayment of the loan? Content vocabulary: deferment, grace period Deferment is the period that he does not have to make payments on the loan principal or interest. Because the loan does not require "In-School Payment," payments will not begin until he is no longer enrolled. Upon leaving school there is a six-month grace period and after the grace period he must begin making monthly payments.
7. Billie is relieved to qualify for a loan, and she wants her part-time job at a fashion boutique to cover interest only payments while she is in school. Which option did she check on the loan application? How is that payment calculated? Content vocabulary: in-school payments Billie checked "In-School Payment" on her loan application. They can be a fixed amount each month or a designated amount toward the interest on the loan. The lender will calculate the payments.
Discussion: How would making "In School Payments" affect the total amount paid over the life of the loan? Would you budget for this option? Why or why not?
8. Ed graduated with a business major and immediately was employed as an accountant. Unfortunately, after two years his company downsized. As the latest hire, he lost his job. He still has 12 years of loan payments, but at this time he cannot afford them. He will need to discuss repayment options with the bank or his loan servicer. Explain forbearance. How will forbearance effect his balance and payments going forward? Content vocabulary: forbearance When the lender grants forbearance, payments are suspended. Interest on the loan still accrues and Ed's loan balance and payment will be higher when he resumes payment because of this added interest.

9. Shawn is trying to decide between a variable and a fixed interest rate for his college loan. Describe the basic differences between fixed and variable rates?

Content vocabulary: fixed interest rate, variable interest rate

A fixed interest rate is set at the time of application and does not change during the life of the loan. The loan payments are fixed also. A variable interest rate may change quarterly during the life of the loan. This may cause the monthly payment to increase, the number of payments to increase, or both.

10. Britney notices the terms “repayment period,” and “default” in her loan note. They are both related to repaying her loan. Explain these terms.

Once the repayment period begins monthly payments are due for the duration of the loan. Should Britney go into default it means she failed to make her scheduled payment and the entire balance of her loan is due.