United States General Accounting Office

GAO

Report to the Ranking Minority Member, Committee on Health, Education, Labor, and Pensions, U.S. Senate

November 2003

DIRECT STUDENT LOAN PROGRAM

Management Actions Could Enhance Customer Service

G A O

Accountability * Integrity * Reliability

GAO-04-107

GAO
Accountability • Integrity • Reliability

Highlights

Highlights of GAO-04-107, a report to the Ranking Minority Member, Committee on Health, Education, Labor, and Pensions, U.S. Senate

November 2003

DIRECT STUDENT LOAN PROGRAM

Management Actions Could Enhance Customer Service

Why GAO Did This Study

In 1993, Congress authorized the William D. Ford Federal Direct Loan Program as an alternative to the Federal Family Education Loan Program (FFELP). While the Direct Loan Program was originally mandated to replace FFELP, Congress revised the law allowing both loan programs to continue. Since that time, competition between the programs has been credited with improving borrower benefits and service for schools. The Department of Education's (Education) Office of Federal Student Aid (FSA) and its contractors administer the Direct Loan Program, and one of its goals is to improve customer service. In light of the upcoming reauthorization of the Higher Education Act (HEA), which authorizes the loan programs, this report examines the extent to which schools participate in the Direct Loan Program, factors that influenced schools' decision to begin—and for some schools end—participation, and steps that FSA has taken to increase the user-friendliness of the program.

What GAO Recommends

Congress should consider clarifying whether Education may regulate the fees charged to borrowers under the Direct Loan Program.

We are also recommending that FSA collect information from schools that could be used to make improvements to the Direct Loan Program. Education agreed with our recommendation.

www.gao.gov/cgi-bin/getrpt?GAO-04-107.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Cornelia Ashby (202) 512-8403.

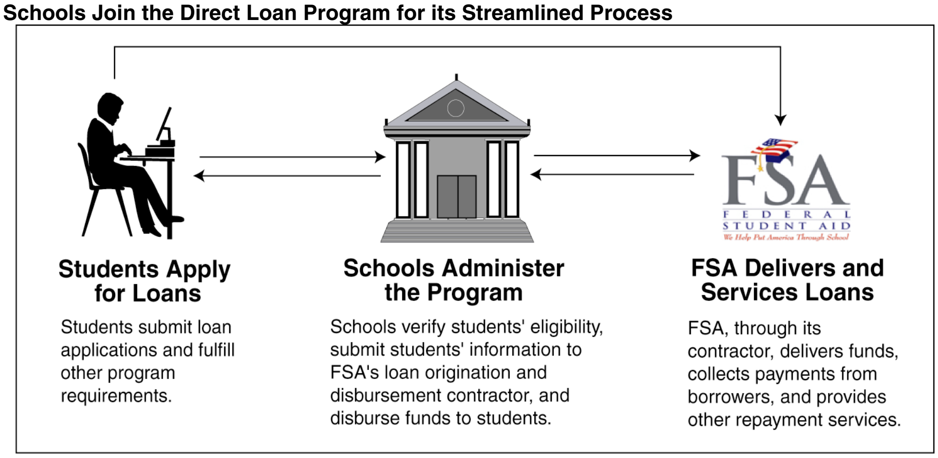
What GAO Found

Of schools that provided federal loans in every year since 1994-95, approximately 1,200 postsecondary schools—or 29 percent—have provided loans through the Direct Loan Program, and most continued to participate in school year 2001-02. The Direct Loan Program's share of total new loan volume has steadily decreased from its peak of 34 percent in 1998-99 to 28 percent in 2001-02, and the number of schools that have joined the program is much smaller than the number of school that have stopped participating.

Four factors—(1) streamlined loan delivery, (2) greater control over loan processes, (3) timely delivery of money to students, and (4) ease of tracking loans over time—were extremely or very important in influencing schools' decision to participate in the Direct Loan Program. Schools that joined and subsequently left the Direct Loan Program reported a number of factors that influenced their decision, including difficulties fulfilling certain program requirements and reduced or no loan origination fees offered by FFELP lenders. Education has reduced origination fees for Direct Loan borrowers, but its regulatory authority to do so has been challenged. FSA does not systematically collect information from schools about the reasons why they stop participating in the Direct Loan Program, although this information could be used to identify needed program improvements.

FSA has taken a number of steps to increase the user-friendliness of the program, such as using Web sites to disseminate and collect information and forms. Many Direct Loan schools reported that FSA's Web sites are effective in helping them administer the program and have simplified the process for Direct Loan borrowers, but it is challenging to navigate among multiple Web sites. FSA officials are aware of schools' concerns and are developing a plan to redesign its Web sites. FSA has also implemented a new information system that originates and disburses Direct Loans to students faster, and 72 percent of Direct Loan schools were generally or very satisfied with this system.

Schools Join the Direct Loan Program for its Streamlined Process



Source: GAO analysis.

Contents

Figures

GAO
Accountability * Integrity * Reliability

United States General Accounting Office
Washington, DC 20548

November 20, 2003

The Honorable Edward M. Kennedy
Ranking Minority Member
Committee on Health, Education, Labor, and Pensions
United States Senate

Dear Senator Kennedy:

In 1993, Congress authorized the William D. Ford Federal Direct Loan Program (Direct Loan Program) as an alternative to the Federal Family Education Loan Program (FFELP). The original legislation authorizing the Direct Loan Program specified that it would gradually expand and replace FFELP, but in 1998 Congress removed those provisions. In the ensuing years, competition between the two loan programs has been credited with improving service for schools and benefits for borrowers. Postsecondary schools may participate in one or both loan programs. Regardless of which program schools use, students and families are eligible for the same types of loans. In school year 2002-03, students and their families borrowed an estimated $12 billion in new loans through the Direct Loan Program and $30 billion through FFELP.

The federal government's role in financing and administering these two loan programs differs significantly. Under FFELP, private lenders, such as banks, provide loan capital and the federal government guarantees FFELP lenders a minimum rate of return on the loans they make and repayment if borrowers default.[1] Additionally, state-designated guaranty agencies perform a variety of administrative functions in FFELP. Under the Direct Loan Program, federal funds are used as loan capital and are provided through participating schools. The Department of Education's Office of Federal Student Aid (FSA) and its private-sector contractors jointly administer the program. FSA is responsible for delivering funds to schools that provide Direct Loans, monitoring its contracts, and facilitating interactions between schools providing Direct Loans and the contractors. In 1998, Congress established FSA as a performance-based organization

[1]For loans disbursed on or after October 1, 1998, the government pays 95 percent of the default costs plus certain administrative costs. The percentage of default costs paid by the federal government decreases if the guarantor's default claims are high compared with the amount of loans in repayment.

with specific purposes, including improving customer service and the information systems FSA uses to administer student loan and other financial aid programs.

As part of the upcoming reauthorization of the Higher Education Act (HEA), you asked us to review the status of the Direct Loan Program by answering the following questions: (1) To what extent have schools participated in the Direct Loan Program? (2) What factors influenced schools' decision to participate in the Direct Loan Program, and if applicable, what factors influenced schools' decision to stop participating? (3) What steps has FSA taken to increase the user-friendliness of the Direct Loan Program for schools and students?

To address the first question, we analyzed data from three Education databases and identified schools that provided loans through either the Direct Loan Program or FFELP in each school year from 1994-95 to 2001-02. To address the second question, we surveyed financial aid officials at schools that participated in the Direct Loan Program in 2001-02, of whom 57 percent responded to our survey. [2] We also surveyed schools that had participated in the program for at least one school year from 1994-95 to 2000-01 but did not participate in 2001-02. Twenty-three percent of these schools responded to our survey, and because of their low response rate we do not provide estimates for this group. We conducted site visits and telephone interviews with 20 Direct Loan public and private, 4-year, 2-year, and less-than-2-year schools located in the Boston, New York, San Francisco, and Washington, D.C., metropolitan areas. These schools were selected on the basis of school type and loan volume. We also interviewed financial aid officials at three schools that had once participated in the Direct Loan Program but were no longer doing so. To learn about benefits available to borrowers, we reviewed the terms of loans provided through the Direct Loan Program as well as the terms of loans provided through selected FFELP lenders. To address the third question, we gathered information about schools' experiences through our survey and site visits at Direct Loan schools. In addition, we

[2] Because of the large proportion of the total population of schools that responded to our survey and the result of our comparison of respondent- and nonrespondent-based estimates, we chose to include the survey results in our report and to project sample-based estimates for the total population of schools in our study population. Percentage estimates for Direct Loan schools are based on the "sample" and are subject to sampling error. Unless otherwise noted, we are 95 percent confident that the results we obtained are within +/- 6 percentage points of what we would have obtained if we had received responses from the entire population. See appendix I for more details.

interviewed FSA staff at headquarters and three regional offices. We also reviewed the Higher Education Act of 1965, as amended, and related regulations; contracts for FSA's information systems; FSA planning documents; and FSA Web sites. We conducted our work from February through October 2003 in accordance with generally accepted government auditing standards.

Results in Brief

Of the schools that provided federal student loans in each year since 1994-95, approximately 1,200—or 29 percent—provided loans through the Direct Loan Program, and most of those schools continued to participate in the Direct Loan Program in school year 2001-02. In 2001-02, public 4-year schools provided the largest share of Direct Loan volume, about $6.9 billion, or 67 percent, although roughly equal numbers of public 4-year, private 4-year, 2-year, and less-than-2-year schools participated. The Direct Loan Program's share of total new loan volume has steadily decreased from its peak of 34 percent in 1998-99 to 28 percent in 2001-02. During this period, only 34 schools began participating in the program, while 166 schools have stopped.

Similar factors influenced a large majority of schools' decision to participate in the Direct Loan Program, whereas the factors that led schools to leave the program varied. Four factors—(1) streamlined loan delivery, (2) greater control over loan processes, (3) timely delivery of money to students, and (4) ease of tracking loans over time—were extremely or very important in influencing 70 percent of Direct Loan schools' decision to participate in the program. While recognizing that improvements have since occurred in FFELP, financial aid officials at Direct Loan schools we visited explained that prior to joining the Direct Loan Program, they had to follow separate and distinct loan processes for each of the many FFELP lenders and guaranty agencies used by their students. In contrast, Direct Loan schools have only one lender—the federal government—and one process to follow. The factors that led many schools to end their participation in the Direct Loan Program varied. For example, some experienced difficulties meeting the Direct Loan Program requirement that they match the school's loan records with the loan origination and disbursement contractor's records and resolve any discrepancies. Other schools stopped participating because some FFELP lenders offered better loan terms for borrowers. For example, some FFELP lenders did not charge borrowers loan origination fees and offered interest rate reductions that were unavailable to the schools' students under the Direct Loan Program.[3] Education has reduced the origination fees for Direct Loan borrowers, but a coalition of FFELP lenders has challenged its regulatory authority to do so and the case is still pending in court. Financial aid officials at Direct Loan schools we visited expressed concern about the continued viability of the Direct Loan Program in light of FFELP lenders' ability to offer more attractive terms to borrowers. The extent to which FFELP lenders will continue to offer such benefits is unknown. FSA does not systematically collect information from schools about the reasons why they stop participating in the Direct Loan Program, although this information could be used to identify needed program improvements.

FSA has made the Direct Loan Program more user-friendly for schools and students by (1) using Web sites to disseminate and collect information and forms, (2) implementing a new information system that originates and disburses Direct Loans to students faster, and (3) providing staff in regional offices to assist Direct Loan schools. Direct Loan schools indicated that FSA's Web sites are effective in helping them administer the program and have simplified the process for Direct Loan borrowers. For example, Direct Loan borrowers are able to complete and sign their loan applications online and view information about their loans when they enter repayment. Despite schools' satisfaction with FSA's Web sites, they reported that it is challenging to navigate among multiple Web sites. FSA officials stated that they are aware of the challenges facing schools and are in the early stages of redesigning their Web sites. Seventy-two percent of Direct Loan schools were generally or very satisfied with FSA's new information system, which originates and disburses loans faster. However, many schools commented that customer service representatives—contractors hired to provide technical assistance to schools—do not know all of the Direct Loan Program's requirements and thus are typically unable to answer their questions. FSA officials reported that they are taking steps to address this issue, such as temporarily reassigning FSA staff to answer telephone inquiries. More than three-quarters of Direct Loan schools were very or generally satisfied with the quality of service provided by the regional office staff. Direct Loan schools commented that training provided by the regional office staff helped them administer the program.

[3] Although FFELP lenders did not charge fees to borrowers, they still paid the loan origination fees to the federal government.

In this report we are suggesting that Congress consider clarifying whether Education may regulate loan origination fees charged to borrowers under the Direct Loan Program. In addition, we are recommending that FSA's Chief Operating Officer take actions to collect information from schools that have left the Direct Loan Program about the factors that influenced this decision, information that could be used to make improvements to the Direct Loan Program, thereby helping FSA meet its goal of improving customer service.

We provided Education with a copy of our draft report for review and comment. In written comments on our draft report, Education generally agreed with our reported findings and recommendation. Education's written comments appear in appendix II. Education also provided technical clarification, which we incorporated where appropriate.

Background

Title IV of HEA authorizes federal student aid programs, including the Direct Loan Program and FFELP. FFELP originated in the HEA of 1965, while the Direct Loan Program was created in 1993. Originally, the Direct Loan Program was expected to replace FFELP over a 5-year period with the amount of loans provided through the Direct Loan Program rising from 5 percent in 1994-95 to 60 percent in 1998-99. In reauthorizing HEA in 1998, Congress removed the provisions that called for the phase-in of the program, thus keeping two federal loan programs. In the ensuing years, competition between the two loan programs has been credited with improving service to schools and benefits for borrowers.

Under the Direct Loan Program, students and families borrow through one lender—the federal government—which also provides repayment services to borrowers. In contrast, students and families can borrow through thousands of FFELP lenders, who may or may not continue to provide repayment services to students and families. FFELP lenders may receive a subsidy, called a special allowance payment, from the federal government to ensure that they receive a guaranteed rate of return on the student loans they make. Additionally, under FFELP, state-designated guaranty agencies perform a variety of administrative functions and guarantee payment to lenders if borrowers fail to repay their loans; the federal government subsequently reimburses guaranty agencies for these payments to lenders.

Borrower and School Benefits

Both the Direct Loan Program and FFELP offer the same loans to students and their families: unsubsidized and subsidized Stafford and PLUS loans, but the loan origination fees and repayment options can differ under each program.[4] HEA specifies loan origination fees of 4 percent in the Direct Loan Program and up to 3 percent under FFELP. Prior to 1998, FFELP lenders had the flexibility to reduce origination fees for subsidized loan borrowers; in 1998, Congress expanded this flexibility to unsubsidized loan borrowers. Although lenders may reduce the fees they charge borrowers, they must still pay the full amount of the fee to the federal government. Under HEA, guaranty agencies also have the option of waiving a 1 percent loan insurance fee charged to borrowers that is used to compensate guaranty agencies for default costs and other claims. Borrowers in the Direct Loan Program and FFELP can choose from three similar repayment plans, including:

- Standard repayment—borrowers pay a fixed monthly amount of at least $50 up to 10 years;
- Graduated repayment—borrowers pay smaller monthly amounts initially and in later years the monthly amount is larger;
- Extended repayment—borrowers pay a fixed monthly amount that can be repaid over a time period as long as 25 years under FFEL and 30 years under the Direct Loan Program.[5]

Last, borrowers in both loan programs have the option of choosing a repayment plan that is adjusted according to the borrower's income, but under the Direct Loan Program borrowers have a longer period of time to repay, and after 25 years of repayment, any remaining amount owed on the loan is discharged.

Another difference between FFELP and the Direct Loan Program is that HEA includes a provision that allows a school to become a FFELP lender

[4]Subsidized Stafford loans are made to students who are enrolled at least half-time and have demonstrated financial need, while unsubsidized Stafford loans are made to any student enrolled at least half-time, and PLUS loans are made to parents of undergraduate students. Unsubsidized and PLUS loan borrowers must pay all loan interest costs, whereas the federal government pays the interest cost of subsidized loans while the student is in school.

[5]The monthly amount paid under the graduated plan and the criteria for who qualifies under the extended plan vary between the Direct Loan Program and FFELP.

to its graduate students.[6] A school may use its own funds to lend to students or, according to one FFELP guaranty agency, the school may receive a line of credit from another FFELP lender and pay interest on the funds as they are used. Under the law, proceeds earned from the special allowance payment and interest payments associated with these loans can be used for need-based grants or administrative expenses. Schools also sell their loans to secondary markets.[7]

Schools' Administrative Responsibilities

Schools choose which federal loan program they will offer to their students and can participate in both. Although a school may provide loans through both the Direct Loan Program and FFELP, the administrative processes are different under each program, with Direct Loan schools assuming additional responsibilities. Under both processes, schools collect and provide data on whether borrowers are eligible to receive loans. Also, schools in both loan programs must counsel students on the responsibilities of borrowing and can use either written materials, an audiovisual presentation, or a Web site.

In the Direct Loan Program, schools are responsible for completing all tasks to originate and disburse loans to students.[8] Furthermore, schools that originate loans in the Direct Loan Program are responsible for completing a monthly loan reconciliation by comparing their internal Direct Loan records with the cash balance reported by FSA's loan origination and disbursement contractor and resolving all differences between the contractor's report and the school's internal records. Schools must also reconcile on a yearly basis. In comparison, as shown in table 1, schools that participate in FFELP share some administrative tasks with lenders and are not required to perform reconciliation.

[6]Schools can act as lenders generally to graduate students and with some limitations to undergraduate students. HEA specifies that a school can act as lender to its undergraduates as long as it does not lend to more than 50 percent of its undergraduates and that it extends loans to students who have previously received a loan from the school or have been rejected by other lenders.

[7]Secondary market lenders include Sallie Mae, banks, and nonprofit state agencies that purchase loans from originating lenders in order to provide additional capital that originating lenders can then use to make new loans.

[8]With the Secretary of Education's approval, schools may choose to use a third-party servicer to administer the Direct Loan Program on behalf of the school.

Table 1: Comparison of Responsibilities for Schools That Participate in the Direct Loan Program and FFELP

Administrative task	Who's responsible in: Direct Loan Program	Who's responsible in: FFELP
Determine students' eligibility for federal loan	School	School
Obtain completed promissory note from borrower	School	Lender
Provide entrance and exit counseling to borrowers	School	School
Disburse money to students	School	Lender and school
Perform monthly loan reconciliation	School	Not required

Source: GAO analysis of FSA and Congressional Research Service documents.

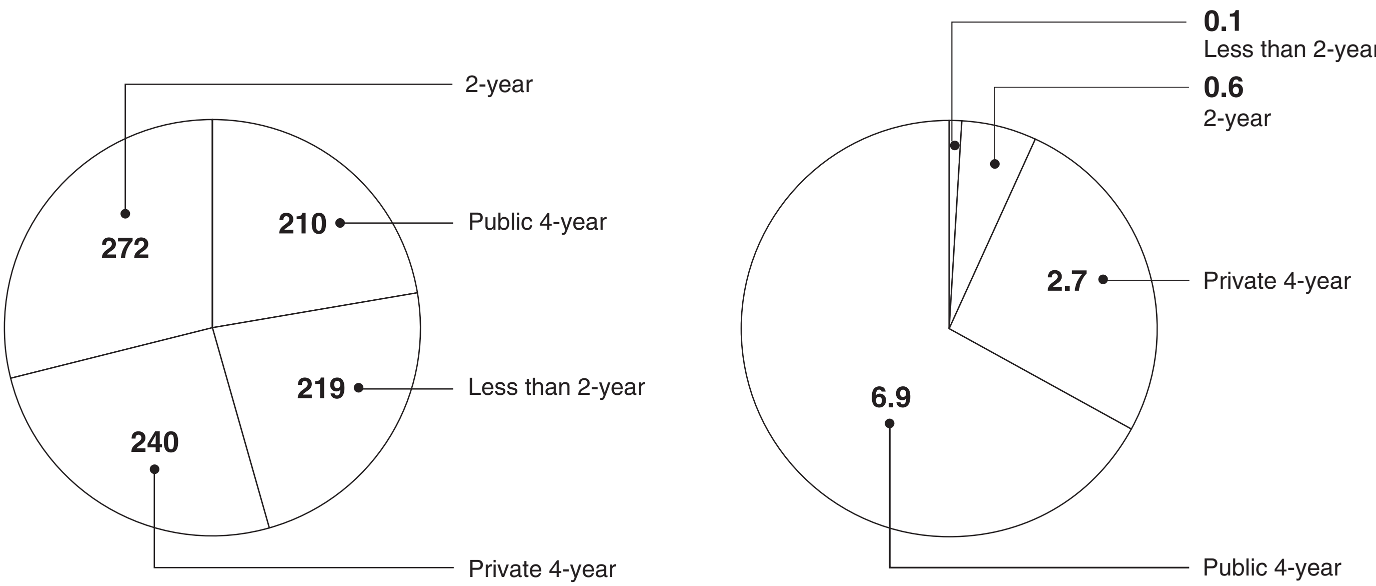
About One-Third of Postsecondary Schools That Provided Federal Loans since 1994-95 Have Participated in the Direct Loan Program

Of the schools that provided federal student loans in each year since 1994-95, approximately 1,200—or 29 percent—provided loans through the Direct Loan Program, and most of those schools continued to participate in the Direct Loan Program in school year 2001-02. Since 1998-99, the Direct Loan Program's share of total new loan volume has steadily decreased from its peak of 34 percent to 28 percent in 2001-02. During this same time period, the number of schools that began to participate in the program was smaller than the number of schools that stopped participating.

Among Schools That Participated in the Direct Loan Program during School Year 2001-02, Public 4-Year Schools Provided Most of the Program's Loan Volume

Of the 941 schools that were still participating in the Direct Loan Program in school year 2001-02, public 4-year schools provided most of the program's loan volume. About an equal number of public and private 4-year, 2-year, and less-than-2-year schools participated in the Direct Loan Program in 2001-02, with many schools beginning participation in the early years of the Direct Loan Program. Public 4-year schools provided the largest share of Direct Loan volume, about $6.9 billion, or 67 percent of total 2001-02 Direct Loan volume (see figure 1).

Figure 1: Number of Direct Loan Schools and Direct Loan Volume (in billions of dollars) in School Year 2001-02, by School Type

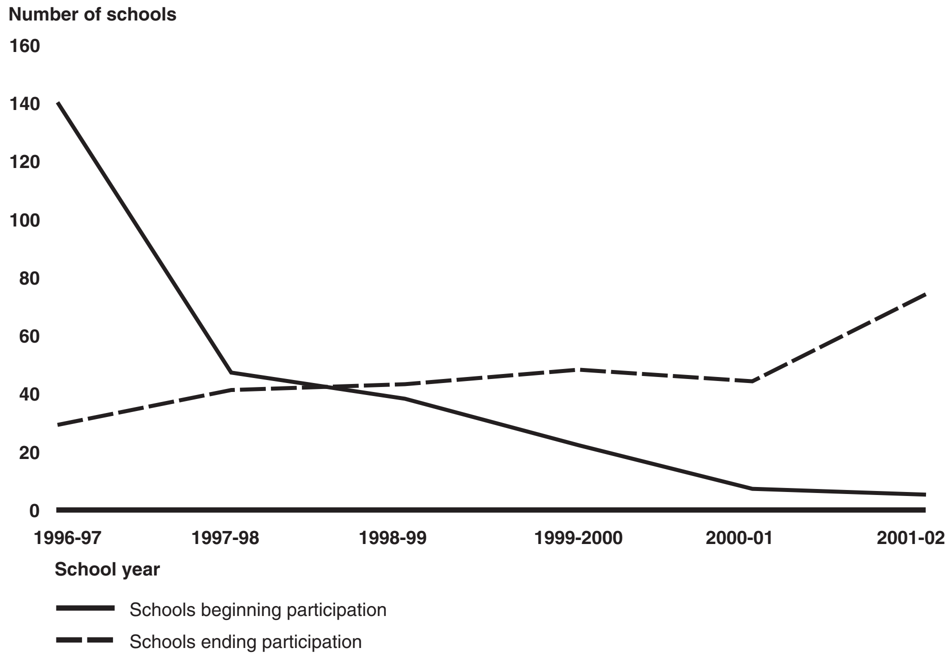


Source: GAO analysis of Education data.

Since 1998-99, More Schools Have Stopped Participating in the Direct Loan Program than Have Joined

Since 1998-99, the number of schools that stopped participating in the Direct Loan Program is greater than the number that have joined. During this same time, the program's share of total new loan volume has decreased, despite annual increases in total Direct Loan volume. As shown in figure 2, 166 schools have stopped participating in the program since 1998-99, while only 34 began participating.

Figure 2: Number of Schools Beginning and Ending Participation in Each School Year between 1996-97 and 2001-02



Source: GAO analysis of Education data.

The small number of schools entering the program after 1998 coincided with a number of changes that occurred at FSA and in FFELP. FSA officials reported that in 1998 they instituted a policy of not marketing the Direct Loan Program and ended activities they designed to promote the Direct Loan Program, such as holding sessions at conferences or visiting financial aid officials to discuss the benefits of the Direct Loan Program. FSA officials reported that at a Direct Loan school's request, they send information detailing how the Direct Loan Program benefits the school's students, and they visit campuses considering leaving the Direct Loan Program to make presentations about the program's benefits. FFELP lenders have continued to market their services to Direct Loan schools. Their efforts include sending mailings to students and inviting financial aid staff to attend information sessions to learn more about switching from the Direct Loan Program to FFELP.

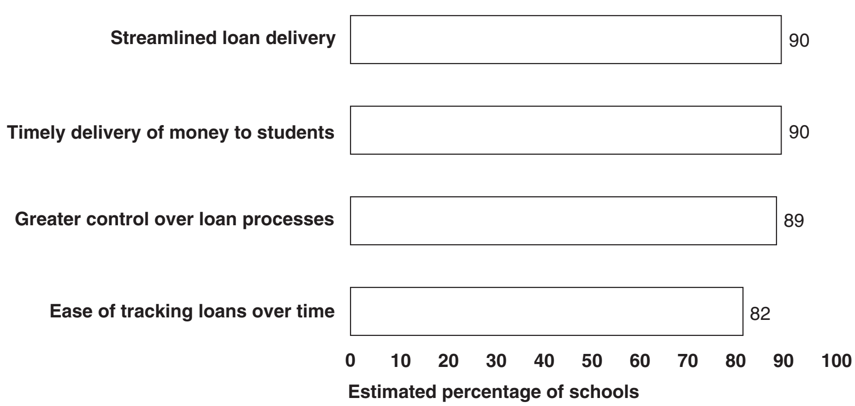
Similar Factors Influenced a Majority of Schools' Decision to Participate in the Program but the Factors That Influenced Schools' Decision to End Participation Varied

Similar factors influenced a large majority of schools' decision to participate in the Direct Loan Program, whereas the factors that led schools to leave the program varied. Four factors—(1) streamlined loan delivery, (2) greater control over loan processes, (3) timely delivery of money to students, and (4) ease of tracking loans over time—were extremely or very important in influencing 70 percent of Direct Loan schools' decision to participate in the Direct Loan Program. The factors that led many schools to end their participation in the Direct Loan Program varied and included, for example, difficulties meeting program requirements, the availability of lower loan origination fees under FFELP, and repayment incentives offered by FFELP lenders, which were unavailable to Direct Loan Program borrowers. FSA does not collect information on reasons why schools stop participating in the Direct Loan Program; thus it may be unaware of improvements that could be made to better serve schools and borrowers.

Four Factors Were Very Important in Influencing Schools' Decision to Participate in the Program

A substantial majority of schools reported that four factors were extremely or very important in influencing their decision to participate in the Direct Loan Program. Figure 3 shows, for each of these factors, the percentage of schools that reported them as very or extremely important.

Figure 3: Factors That Were Extremely or Very Important in Schools' Decision to Join the Direct Loan Program

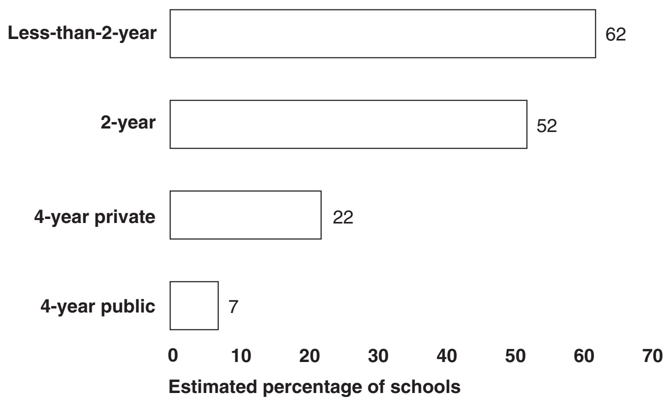


Source: GAO Survey of Postsecondary School Experiences with the Direct Loan Program.

Although financial aid officials at Direct Loan schools we visited acknowledged improvements in FFELP, they commented that prior to joining the Direct Loan Program, they had to learn and follow separate and distinct loan processes for each lender and guaranty agency that was used by their students and their parents. In contrast, the loan delivery process under the Direct Loan Program is streamlined: there is only one lender—the federal government—and a uniform process. Financial aid officials also noted that under FFELP, students often did not receive their loans in a timely matter, in some cases waiting 6 weeks after school began to receive funds. Under the Direct Loan Program, they said, students received their loans quickly. Once again, financial aid officials noted that FFELP lenders have improved in this area as well. Financial aid officials at Direct Loan schools also told us that a third factor—greater control over loan processes—was important because in the Direct Loan Program schools were directly responsible for ensuring that an eligible student received a loan, whereas in FFELP, schools were dependent on lenders or guaranty agencies to approve a student's loan before a student could receive the money. Moreover, school financial aid officials said that under the Direct Loan Program they were also able to easily change the amount of a loan if needed. For example, schools can adjust the amount of a Direct Loan to reflect changes in students' courseload or increases in grant and scholarship aid—events that could affect the loan amount available to borrowers. The fourth factor—ease of tracking student loans over time—was important because the Direct Loan Program improved the loan process for students. Under the Direct Loan Program, for example, student borrowers could easily track their loans because the same lender held the loans through repayment, which was often not the case under FFELP. Financial aid officials at a few schools associated students' ease of tracking loans with reductions in default rates on their campuses.

While another factor—the availability of lenders willing to lend to a school's students—was reported by about 36 percent of Direct Loan schools as extremely or very important, responses varied by school type. In particular, as shown in figure 4, for a higher percentage of 2-year and less-than-2-year schools the factor was extremely or very important.

Figure 4: Estimated Percentages of Schools for Which the Availability of Lenders Willing to Lend to Their Students Was an Extremely or Very Important Factor in Influencing Schools' decision to Join Direct Loan Program, by School Type



Source: GAO Survey of Postsecondary School Experiences with the Direct Loan Program.

Note: The 95-percent confidence interval for the estimated percentage of less-than-2-year schools is from 56 to 69 percent.

According to financial aid officials at 2-year and less-than-2-year schools we visited, prior to the Direct Loan Program, some FFELP lenders refused to lend to students at their schools because some of their graduates did not repay their loans on time. In contrast, financial aid officials at public and private 4-year schools we visited said that they did not have any problems finding lenders to serve their students, and FFELP lenders actively marketed their products to them and their students.

Thirty-nine percent of schools that participated in the Direct Loan Program in 2001-02 also participated in FFELP and provided a number of reasons for doing so. Some schools participated in FFELP, in addition to the Direct Loan Program, to provide PLUS loans to parents. Some financial aid officials reported that parents receive better terms for PLUS loans through FFELP. For 57 percent of schools that participated in both loan programs, maintaining relationships with lenders was an extremely or very important factor in influencing this decision. Through our site visits we learned that some schools do this to establish relationships with lenders in order to allow students access to alternative loans and make the transition to FFELP smoother in case the Direct Loan Program is eliminated. Finally, some schools provided most of their loans through FFELP but wanted to allow students that transferred to their school with a Direct Loan the option of continuing to borrow through the Direct Loan Program.

A Variety of Factors Influenced Schools' Decision to End Participation in the Direct Loan Program

A number of schools that joined the Direct Loan Program but subsequently stopped participating reported that different factors influenced their decision to do so. Some of these factors were related to schools' experiences meeting Direct Loan Program reconciliation requirements or having staff with technical expertise to administer the program. For example, over half of the 61 former Direct Loan schools that responded to our survey reported that the amount of time spent on loan reconciliation, a requirement only schools participating in the Direct Loan Program must meet, was extremely or very important in influencing their decision to leave the program. Schools reported that complying with the requirement to reconcile schools' records with contractors' records was challenging because sometimes the contractor had incorrect information and resolving those differences was time-consuming and frustrating. Although many schools reported that the loan reconciliation process was challenging, we learned during our site visits and from FSA officials that schools that established internal "checks and balances" and meticulously organized their loan information could more easily complete the loan reconciliation process.

Another important factor for leaving the program reported by former Direct Loan schools responding to our survey and through our interviews was that some FFELP lenders offered better loan terms for their students and parents in 2003 than those offered by the Direct Loan Program. For example, many FFELP lenders offered loans with reduced or no origination fees and the potential for interest rate reductions that were unavailable to the schools' students under the Direct Loan Program. For both loan programs, borrower interest rates are variable and change annually based on prevailing market rates, in accordance with the law.[9] Lenders have the flexibility, however, to offer borrowers lower rates. Moreover, all but two guaranty agencies did not charge student borrowers the loan insurance fee, thus lowering costs for almost all borrowers in FFELP. As shown in table 2, financial benefits available to borrowers may vary by program and lender.

[9] Under the law, the maximum borrower rate for Stafford loans is based on the 91-day Treasury-bill rate plus 1.7 percent while students are in school or plus 2.3 percent if a student's loan is in repayment, capped at 8.25 percent.

Table 2: Fees and Repayment Incentives Available to Borrowers in the Direct Loan Program and Selected FFELP Lenders in 2003

Lender	Origination fee	Repayment incentives
Department of Education (Direct Loan Program)	3% (Stafford loan) 4% (PLUS loan)	• 0.25% interest rate reduction for repaying electronically • 1.5% rebate of loan amount borrowed applied at the time loan is disbursed. Borrowers must make 12 consecutive on-time payments or amount will be added back to borrower's account.
FFELP lender A	0% (Stafford loan) 3% (PLUS loan)[a]	• 0.25% interest rate reduction for repaying electronically • PLUS loans interest-free for the first year • portion of loan debt cancelled when student graduates with degree; amount varies by degree type • 2% rate reduction for 48 consecutive on-time monthly payments
FFELP lender B	0% (Stafford loan) 3% (PLUS loan)[a]	• 0.25 % interest rate reduction for repaying electronically • interest rate reduced to 0% after 36 monthly on-time payment for Stafford or PLUS loans
FFELP lender C	Up to 3% (Stafford and PLUS loans)	• 0.25% interest rate reduction on PLUS loans for repaying electronically if serviced by a specific servicer • 3.3% credit or cash rebate on principal balance of Stafford loans if loans are serviced by a specified servicer, borrower agrees to have account information available at a valid e-mail account, and initial 33 payments are made on time
FFELP lender D	3% (Stafford and PLUS loans)	• 0.25 % interest rate reduction for repaying electronically • credit on origination fees if Stafford loans are owned and serviced by lender minus $250 after the first 24 consecutive payments • 2% interest rate savings after first 48 months of on-time payments if loan is owned and serviced by lender

Source: GAO analysis of borrower benefits under the Direct Loan Program and selected FFELP lenders.

[a] PLUS loan origination fees are credited back to the borrower's account.

Note: FFELP lenders include banks and guaranty agencies that also serve as lenders.

Although FFELP lenders can offer reduced fees and other benefits to borrowers, they are not obligated to do so every year. FFELP lenders' decision to offer such benefits to borrowers may depend on a variety of factors, such as lenders' cost for each loan dollar and lenders' ability to link the benefits to borrower behavior. For example, lenders with relatively low costs for each loan dollar might decide to pass these savings on to borrowers. FFELP lenders might also choose to offer such benefits only to select borrowers that exhibit certain repayment behavior, such as those who make consecutive on-time repayments. According to some lenders, the number of borrowers who receive benefits because they satisfy such repayment requirements may be low.

In order to compete with FFELP lenders, Education reduced its origination fees in 1999 for Direct Loan borrowers and, as a repayment incentive, offered an interest rate reduction for borrowers who repay electronically, but its authority to lower origination fees has been challenged. When taking these actions, Education cited an HEA provision that states Direct Loan Program borrowers are to receive the same terms and conditions as FFELP borrowers. A coalition of FFELP lenders filed a lawsuit challenging Education's regulatory authority to reduce origination fees because HEA also includes a provision that sets the Direct Loan Program origination fee at 4 percent.[10] At this time, the case is still pending. Given the differences in fees and other benefits offered to students through FFELP, financial aid officials at Direct Loan schools we visited expressed concern about the continued viability of the Direct Loan Program in light of FFELP lenders' ability to offer more attractive loan terms to borrowers. Some financial aid officials we interviewed suggested that Education further reduce or eliminate loan origination fees for Direct Loan borrowers. Because loan origination fees offset federal loan program costs, any changes to the amount of origination fees charged to borrowers may affect federal costs.[11]

[10]*Student Loan Finance et al. v Riley, Civ. A. No. 2660 (D.D.C. 2000)*. In response to a congressional request before the litigation was filed, GAO issued an opinion finding that Education lacked authority to reduce the 4 percent loan origination fee B-238717, Sept. 29, 1999.

[11]When Education lowered fees in 1999, Education officials reported in its report *Cost of the 1999 Reduction in Direct Loan Fees* that the fee reduction would increase the cost of the Direct Loan Program. However they believed that the increase would be offset by the ability to attract new borrowers to the Direct Loan Program who might otherwise obtain loans from the more costly FFELP, whose lenders were offering fee discounts to attract borrowers.

In addition, more recently some schools have switched from the Direct Loan Program to FFELP in order to become lenders to the schools' graduate students—an option not available under the Direct Loan Program. A large public 4-year Direct Loan school in the Midwest recently entered into such an agreement with a coalition of FFELP lenders for school year 2003-04 in which it would end its participation in the Direct Loan Program and the school would serve as a lender to its graduate students. Under the agreement, the school agreed that the lender coalition would be the preferred lender for its undergraduates.[12] In return, students pay no origination fees and receive other repayment incentives. Financial aid officials at several Direct Loan schools with graduate students reported that FFELP lenders have contacted them and their schools' executive officers about the financial benefits available to a school that becomes a lender to its graduate students. Although these schools have not switched from the Direct Loan Program to FFELP, they reported that they are considering the opportunity to earn money as school lenders.

FSA Does Not Collect Information on the Factors Influencing Schools' Decision to Stop Participating

FSA does not systematically collect information about the factors that influence schools' decision to stop participating in the Direct Loan Program, although this information could be used to identify needed program improvements. Current regulations require schools to notify the Secretary of Education of their intent to leave the Direct Loan Program, and after 60 days, or at an earlier time if the Secretary agrees, they can stop participating. However, FSA officials reported that they typically learn schools have stopped participating when schools stop disbursing funds through the Direct Loan Program. Although schools may send letters detailing why they have stopped participating, such letters may not always be sent to the same office within FSA. FSA may also learn about factors that influence some schools' decision to stop participating in the Direct Loan Program from schools that provide such feedback via regularly scheduled conferences and focus groups convened by FSA, which, among other things, provide forums for schools to provide suggestions for improving the program. However, FSA officials reported that they neither routinely nor systematically collect information on the specific reasons why schools decide to stop participating in the program. As a result, FSA may not be aware of improvements that could be made to the program,

[12]Schools that participate in FFELP may designate one or more lenders as a preferred lender from which students can borrow.

which, in turn, might help FSA achieve its goal of improving customer service.

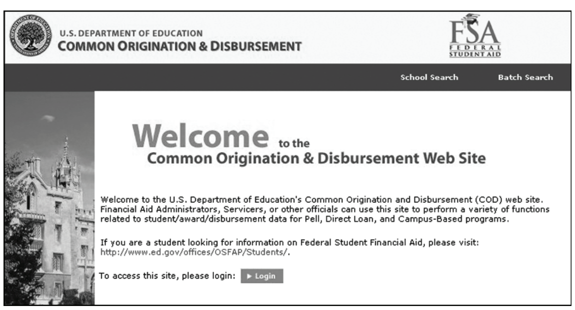
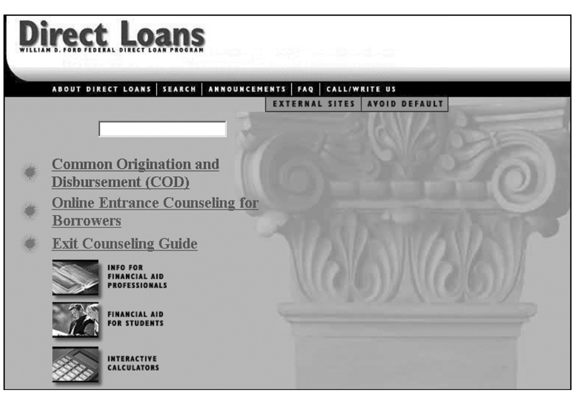
Direct Loan Schools Are Satisfied with Steps Taken by FSA to Make the Program User-Friendly but Identified Opportunities for FSA to Improve These Services

FSA has made the Direct Loan Program more user-friendly for schools and students by (1) using Web sites to disseminate and collect information and forms, (2) implementing a new information system to originate and disburse Direct Loans, and (3) designating regional staff to assist Direct Loan schools. Direct Loan schools indicated that FSA's Web sites are effective in helping them administer the program, but that navigating among the numerous Web sites can be difficult. FSA officials stated that they are aware of schools' concerns and are developing a strategy to redesign its Web sites. Direct Loan schools were also generally satisfied with FSA's information system for originating and disbursing loans, but they have encountered difficulties with customer service representatives who are unable to help them resolve their problems. Finally, FSA regional staff have provided training and technical assistance to Direct Loan schools, and about three-quarters of Direct Loan schools were very or generally satisfied with the quality of service provided by the regional staff.

Direct Loan Schools Reported That FSA's Web Sites Have Helped Them Administer the Program, but Navigating among Multiple Sites Can Be Challenging

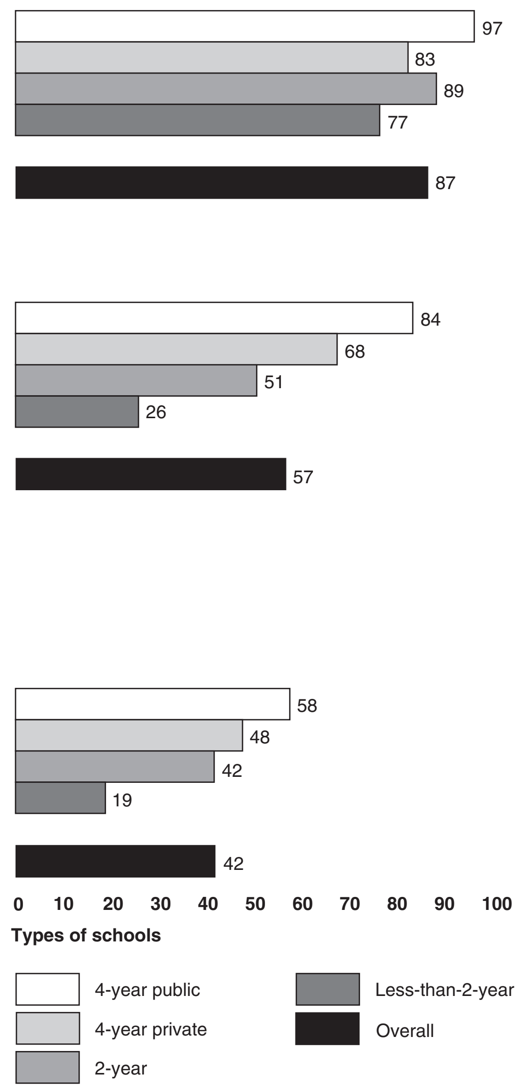
Many Direct Loan schools reported on our survey that FSA's Web sites helped them administer the Direct Loan Program but that navigating among FSA's Web sites was challenging. Schools reported that the Web sites were effective in that they helped them perform various administrative functions, such as determining student eligibility for Direct Loans. Figure 5 provides information about key Web sites FSA developed for schools, the purpose of the Web sites, and the extent to which Direct Loan schools reported using the Web sites very often or often.

Figure 5: Estimated Percentages of Direct Loan Schools' Usage of Certain FSA Web Sites

FSA school Web sites	Purpose
 https://www.nsldsfap.ed.gov/secure/logon.asp	**NSLDS** Schools verify students' eligibility to receive loans and view loan history.
 https://cod.ed.gov/cod/LoginPage	**Common Origination and Disbursement** Schools can view and process data for Direct Loan and other student aid programs and obtain technical assistance.
 http://www.ed.gov/DirectLoan	**Direct Loan home page** Schools can review information and guidance specific to the Direct Loan program.

Survey results

Estimated percentage of Direct Loan schools that reported using Web sites very often or often



Sources: GAO Survey of Postsecondary School Experiences with the Direct Loan Program and U.S. Department of Education, Office of Federal Student Aid, Washington, D.C.

Note: During FSA's transition to a new loan origination and disbursement system, there were two Web sites that schools could use to process and view loan information; these results are related to the Web site for FSA's newly implemented system—the Common Origination and Disbursement (COD).

The various school types reported Web site usage that differed. For example, a larger percentage of 4-year public and private schools reported that they used the NSLDS Web site very often or often than did less-than-2-year schools. At a large public 4-year school with a number of satellite campuses worldwide, financial aid officials stated that the ability to use FSA's Web sites to verify that students have met certain program requirements has been useful because many of its students are unable to visit the financial aid office in person. Almost 64 percent of less-than-2-year schools[13] reported that a corporate office or a third party servicer[14] handled the administrative processes for the Direct Loan Program, thus they did not need to use the Web sites. Furthermore, some schools were not aware of all the FSA Web sites that provided information about the Direct Loan Program.

Additionally, Direct Loan schools reported that FSA Web sites provided relevant and timely information, answered their questions, and were easy to understand. For example, as shown in table 3, 91 percent of Direct Loan schools reported that the NSLDS Web site provided relevant information.

Table 3: Estimated Percentages of Direct Loan Schools' Opinions about FSA Web Sites for Schools

	Estimated percentage of Direct Loan schools that reported Web sites were excellent or good in			
FSA Web sites for schools	**Providing relevant information**	**Providing timely information**	**Answering questions**	**Using language that is easy to understand**
NSLDS https://www.nsldsfap.ed.gov/secure/logon.asp	91	81	70	86
Common Origination and Disbursement Ihttps://cod.ed.gov/cod/LoginPage **Direct Loan Servicing Online** https://schools.dssonline.com/index.asp	73	69	63	72
Direct Loan home page http://www.ed.gov/DirectLoan	80	78	68	84

Source: GAO Survey of Postsecondary School Experiences with the Direct Loan Program.

Note: We asked schools to evaluate the COD and Direct Loan Servicing Online Web sites together.

[13]The 95-percent confidence interval for this estimate is from 56 to 72 percent.

[14]A third party servicer is an individual, a state, or a private—for-profit or nonprofit—organization that enters into a contract with Title IV-eligible institutions to administer the school's Title IV program.

Despite overall satisfaction with FSA's Web sites, many Direct Loan schools reported during our site visits and through our survey that it is challenging to navigate among multiple Web sites because many of the sites require separate passwords. Almost 90 percent of Direct Loan schools believe developing a single password to access all FSA Web sites would have a generally or very positive effect on the Direct Loan Program. Some schools we visited stated that in order to keep track of the many passwords and different expiration dates associated with the passwords, they have stored passwords on personal electronic devices or created easily retrievable documents that list all passwords—actions that could compromise the security of financial information. FSA officials told us that they are aware of the challenges facing schools and are in the early stages of redesigning how they use Web sites to present information and services. This strategy will attempt to address schools' concerns about multiple passwords as well as enhance security by increasing FSA's ability to verify schools' access to and use of data. Further, FSA officials reported that they will continue to collect feedback from schools that submit comments at its Web sites as well as those that attend sessions at FSA-sponsored conferences and focus groups held to discuss their strategy. FSA expects to implement its new Web site strategy by 2006. During the course of our review, FSA developed interim measures linking two of its Web sites—Direct Loan Servicing's Online School site and the Common Origination and Disbursement (COD) site—with one password in an effort to improve customer service.

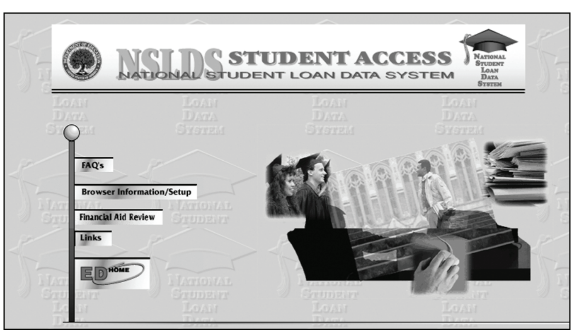
In addition to developing Web sites geared to financial aid administrators, FSA has also developed Web sites that students can use to apply for financial aid, fulfill requirements for receiving a Direct Loan, and monitor their loans from disbursement through repayment. For example, students can access a Web site that allows them to electronically sign a master promissory note, a legally binding agreement between students and Education that outlines the terms and conditions of a Direct Loan. As shown in figure 6, almost half of Direct Loan schools referred their students often or very often to the Direct Loan Servicing Online Web site.

Figure 6: Estimated Percentages of Direct Loan Schools That Refer Their Students to Certain FSA Web Sites

FSA student Web sites

http://www.dlssonline.com/index.asp

https://lo-online.ed.gov/empn/unsecure/



http://www.nslds.ed.gov

Purpose

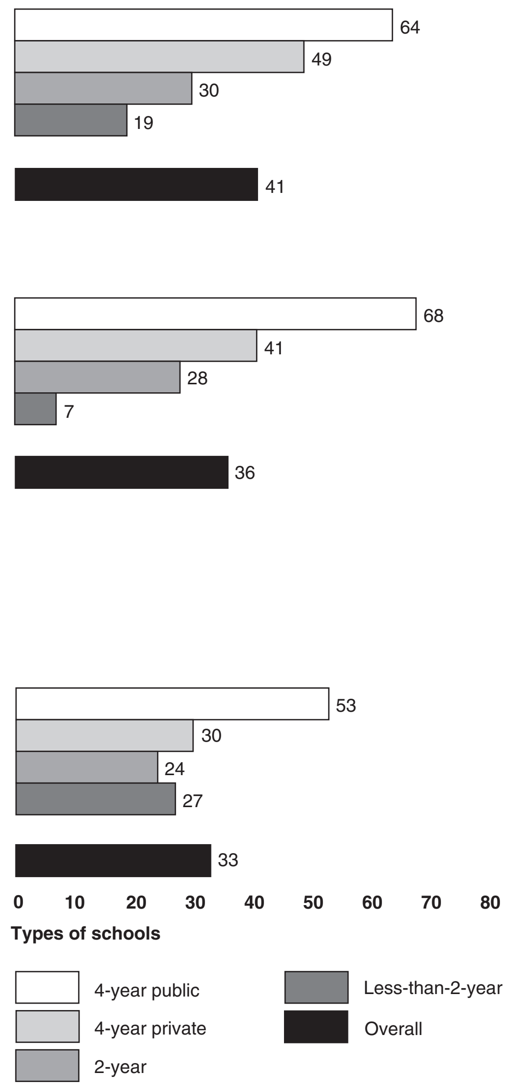
Online Direct Loan servicing
Students can fulfill requirements that they understand the responsibilities of borrowing. Students can also access this site to obtain information about repayment options and electronically repay their loans.

Electronic promissory note
Students or parents can electronically sign master promissory note.

NSLDS
Students can review information regarding their loan and financial aid history.

Survey results

Estimated percentage of Direct Loan schools that report referring students to Web sites very often or often



Sources: GAO Survey of Postsecondary School Experiences with the Direct Loan Program and U.S. Department of Education, Office of Federal Student Aid, Washington, D.C.

Schools that prefer to have their students complete many tasks with paper materials reported a number of reasons for doing so. Financial aid officials at two Direct Loan schools we visited told us that they use paper master promissory notes because they believed it is important for students to sign an actual piece of paper to emphasize the responsibility associated with borrowing. Another school said that their students did not have access to computers at home and the school had a limited number of computers on campus, making it necessary for students to complete paper forms to meet program requirements.

Despite the fact that some schools still rely on paper records, some Direct Loan Program materials were sometimes unavailable. Additionally, some financial aid officials told us that many Direct Loan-specific publications, such as brochures used to describe the program to students, have either been discontinued, or are available only online, or have not been updated in several years. Moreover, several Direct Loan schools reported that critical documents, such as the master promissory note, were not available in time for the 2002-03 school year. FSA officials reported that there were delays in distributing paper master promissory notes to schools because the process needed to obtain departmental approval is lengthy. These materials were ready for the 2003-04 school year.

Direct Loan Schools Were Generally Satisfied with FSA's New Information System, which Delivers Loans Faster to Students

Seventy-four percent of Direct Loan schools were generally or very satisfied with FSA's newly implemented information system, known as COD, which delivers loan funds quicker to students.[15] FSA officials indicated that COD is able to process loans quicker than the former loan origination system, with loans made available to schools and borrowers the same day. During our site visits, some Direct Loan schools agreed that they received loan funds faster under the COD system and liked COD features that allowed them to make changes to student loan amounts instantaneously. For example, a 4-year public school in California commented that, due to the state's budget crisis, tuition and fees charged to students will increase in school year 2003-04 and with COD they will be able to make changes to students' loan amounts that will allow students to pay their tuition bills on time.

[15] As part of its goal to integrate its systems, FSA has implemented COD to combine two different information systems previously used to originate and disburse Direct Loans and Pell Grants—federal grants awarded based on students' financial need. All schools must be full participants in COD by 2005-06.

Although schools are satisfied with COD, many reported that customer service representatives designated to handle their questions are typically unable to resolve their problems. FSA has contracted with a private sector organization—Affiliated Computer Systems, Inc.—to hire and manage customer service representatives.[16] This is the third time that FSA has changed contractors to operate the customer service centers. Several Direct Loan schools reported that the customer service representatives are friendly and responsive but typically lack the knowledge of Direct Loan Program requirements needed to resolve schools' issues. For instance, financial aid officials reported difficulties in trying to resolve differences between school records and COD data on whether students had completed the master promissory note. In addition, several Direct Loan schools reported particular problems performing monthly reconciliation of their Direct Loan accounts. For example, one school mistakenly disbursed loan funds for the same student twice, and the customer service representatives were unable to help them correct this mistake. A previous study of the Direct Loan Program in 1998 also highlighted schools' frustration with customer service representatives during past transitions between contractors.[17]

FSA officials acknowledged that they may have to rethink their approach to providing customer service for their loan origination and disbursement systems in order to minimize problems schools encounter when switching contractors. Moreover, FSA officials also acknowledged that they may have underestimated the skills needed by representatives hired to answer questions about COD. FSA officials have taken additional steps to address schools' concerns about the customer service representatives, including temporarily reassigning FSA regional staff to answer telephone inquiries and providing additional training to COD customer service representatives. As outlined in its COD contract, FSA has surveyed schools to gather information about their experiences with COD and will take further action once it has analyzed data obtained in its survey.

[16]Another contractor, TSYS, is responsible for designing and operating the COD system.

[17]Macro International, Inc., *Direct Loan Program Administration: 1993-1998*, (Washington, D.C. 1998).

FSA's Regional Offices Offer Direct Loan Schools Training, Technical Assistance, and Other Services

FSA staff in regional Direct Loan School Relations Offices (DLSRO) have provided training, technical assistance and software support, and answered queries. For about 43 percent of Direct Loan schools, the major reason they contacted FSA regional office staff in school year 2001-02 was to receive technical assistance specific to Direct Loans. Further, 82 percent of Direct Loan schools were very or generally satisfied with DLSRO, and about three-quarters were very or generally satisfied with the quality of service provided by the DLSRO staff. For example, several financial aid officials at schools we visited reported that the training offered by DLSRO staff is helpful and assists them in administering the program.

According to DLSRO officials, the level of assistance that they provide to schools can vary. A DLSRO official reported that over time, as some schools have become more familiar with administering the Direct Loan Program, they have tended to need less intensive services. Other DLSRO officials stated that some schools require intensive assistance to establish processes and systems so that they can meet Direct Loan reconciliation requirements. Some DLSRO staff told us that in recent years budget constraints have limited their ability to conduct on-site visits with Direct Loan schools. To provide services to schools, DLSRO staff organized training sessions at a location convenient for several schools to attend, thus maximizing the efficiency of the training. Although some schools have reported that they are more comfortable administering the program, they continue to use DLSRO staff for services, such as training and help reconciling their accounts. A few Direct Loan schools that we visited reported that they often attend training held at the regional office because they are unable to attend FSA's national conferences. Moreover, one school told us that during the transition to COD, DLSRO staff have been able to address many questions related to the program that the contractor was not equipped to handle because the contractor was unfamiliar with the issues involved.

In July 2003, FSA reorganized its staff in headquarters and in the regional offices to improve its program delivery and customer service. Under the reorganization, DLSRO has been renamed the School Relations Office, and its mission has been broadened from assisting Direct Loan schools to assisting all schools participating in Title IV programs. FSA officials reported that this change was made because the number of schools participating in the Direct Loan Program has decreased and they believed that schools in the Direct Loan Program no longer need individual attention. To address agency needs, several former DLSRO staff have been temporarily reassigned to other offices, where they perform such tasks as providing training to COD contractor staff, developing FSA program software, or working in FSA headquarters operations. FSA officials reported that changes under the reorganization would not adversely affect customer service provided to Direct Loan schools.

Conclusions

The creation of the Direct Loan Program as an alternative to FFELP has provided schools with a choice of programs to provide federal loans to their students. Many financial aid officials believe that competition between the two loan programs has improved service for schools and borrowers. While some schools have recently begun to participate in the Direct Loan Program, others that began participating several years ago have recently stopped. Some schools have stopped participating because some FFELP lenders offered better loan terms—including reduced origination fees and the potential for reduced interest rates—to their students. Not all FFELP lenders offer these better terms nor are they obligated to do so. Further, lenders' willingness and ability to offer these better terms can be contingent on a number of economic factors, including lender costs and the extent of competition in the marketplace. Whether some lenders will continue to provide better loan terms for students in the future is unknown. Nonetheless, schools that remain in the Direct Loan Program have expressed concerns about the continued viability of the program in light of the better benefits offered by some FFELP lenders and the lack of clarity over whether Education may offer similar benefits. In addition to the availability of better loan terms for students under FFELP, schools have also stopped participating in the Direct Loan Program for other reasons. Because FSA does not routinely collect information about why schools stop participating in the program, it is missing an important opportunity to learn whether it could make changes or improvements to the Direct Loan Program that would better serve its customers.

Matters for Congressional Consideration

In light of questions about provisions in the HEA concerning Direct Loan Program origination fees, Congress should consider clarifying the extent to which Education may regulate the loan origination fees charged to borrowers during its reauthorization of the HEA.

Recommendation for Executive Action

To improve knowledge of its Direct Loan customers and meet its goal of increasing customer satisfaction, we recommend that FSA's Chief Operating Officer develop a process for collecting information from schools that decide to stop participating in the Direct Loan Program about the factors that influenced this decision and use this information to make improvements to the program.

Agency Comments

We provided a draft of this report to Education for review and comment. In written comments on our draft report, Education generally agreed with our reported findings and recommendation. Regarding our finding that Education does not collect information from schools that have stopped participating in the program, Education agreed but suggested we acknowledge that Education does provide forums for schools to provide suggestions for improving the Direct Loan Program. In response, we noted on page 17 that conferences and focus groups convened by FSA provide such forums. In response to our recommendation, Education stated that in the future, it would conduct exit interviews of schools leaving the Direct Loan Program and use the information as appropriate. Education also provided technical clarification, which we incorporated where appropriate. Education's written comments appear in appendix II.

We are sending copies of this report to the Secretary of Education, appropriate congressional committees, and other interested parties. In addition, the report will be available at no charge on GAO's Web site at http://www.gao.gov.

If you or your staff have any questions about this report, please call me on (202) 512-8403 or Jeff Appel on (202) 512-9915. Other contacts and staff acknowledgments are listed in appendix III.

Sincerely yours,

Cornelia M. Ashby

Cornelia M. Ashby
Director, Education, Workforce,
and Income Security Issues

Appendix I: Scope and Methodology

To address our research objectives, we analyzed loan volume data and identified schools that participate in the Direct Loan Program or Federal Family Education Loan Program (FFELP), surveyed financial aid directors at schools that have participated in the Direct Loan Program, analyzed information on financial benefits provided by lenders, conducted site visits to Direct Loan schools that were selected based on a variety of criteria, and interviewed by telephone financial aid officials at schools that either were participating in or had participated in the Direct Loan Program.

Analyzing Loan Volume and Identifying Schools That Participated in the Direct Loan Program and FFELP

To identify loan volume and schools that have provided loans through the Direct Loan Program or FFELP, we analyzed institutional-level data on loans in three Department of Education databases—(1) the Committed Loan Volume Report, which includes loan data reported by schools and contractors; (2) the National Student Loan Data System (NSLDS), a national repository of information about federal loans and grants awarded to students; and (3) the Integrated Postsecondary Education Data System (IPEDS), a collection of information obtained from surveys of all institutions whose primary purpose is to provide postsecondary education and provides institutional-level data for a variety of characteristics. The Committed Loan Volume Report was used to determine the loan volume and schools in the Direct Loan Program for school years 1994-95 to 2001-02. NSLDS was used to determine the loan volume and schools in FFELP. IPEDS was used to identify school characteristics. To assess the reliability of the Committed Loan Volume Report, NSLDS, and IPEDS, we reviewed existing information about the data, including documentation produced by officials at Education. Education officials also reported performing data accuracy, validity, and integrity tests to ensure data are reliable. We performed validity tests of key variables. We determined that the Direct Loan, NSLDS, and IPEDS data were sufficiently reliable for our purposes.

We used Education's Office of Postsecondary Education's identification number (OPEID) to match data in each database and excluded all foreign schools. We also excluded schools that did not provide loans through either program in any year between school years 1994-95 and 2001-02. After applying our criteria, we identified 4,155 schools that provided subsidized Stafford, unsubsidized Stafford, or PLUS loans through the Direct Loan Program or FFELP from school years 1994-95 through 2001-02. We classified schools into three categories:

- FFELP school—2,935 schools provided loans through FFELP and never participated in the Direct Loan Program.

- Direct Loan school—941 schools participated in the Direct Loan Program in school year 2001-02. Of schools in this category, 366 also provided loans through FFELP in 2001-02.
- Former Direct Loan school—279 schools participated in the Direct Loan Program for at least one school year from 1994-95 to 2000-01 but not in school year 2001-02. These schools provided loans through FFELP in 2001-02.

Survey of Schools That Have Participated in the Direct Loan Program

We administered a Web survey to financial aid officials at schools we identified as participating in the Direct Loan Program from the 1994-95 to 2001-02 school years. These schools consisted of four school types: 4-year public, 4-year private, 2-year, and less-than-2-year schools. We excluded a small number of schools from the population, and e-mailed the survey to all remaining 1,196 schools in our study population.[1] We conducted the survey between June and August of 2003.

Because most of our survey questions asked schools about their experiences in the Direct Loan Program in 2001-02, we divided the study population into two groups—Direct Loan and former Direct Loan schools. We obtained responses from 57 percent of Direct Loan schools and 23 percent of the former Direct Loan schools. Because of the low response rate of former Direct Loan schools, we do not produce estimates for this group of schools in this report.[2]

Table 4 summarizes the population size of and responses received from Direct Loan schools, by school type.

[1]We did not include 24 schools in our survey because we could not locate correct email addresses. Eighteen of the 24 schools no longer participated in the program in 2001-02. The other 6 schools participated in the program in 2001-02 but their omission does not affect our findings.

[2]In some instances we report the number of former Direct Loan schools responding to a question, but this should not be interpreted as an estimate of the broader population.

Table 4: Response Rates of Schools That Participated in the Direct Loan Program in 2001-02

School type	Direct Loan school population	Number of Direct Loan schools that responded to survey	Percentage of schools responding
4-year public	210	141	67.1
4-year private	240	133	55.4
2-year	268	153	57.1
Less-than-2-year	217	110	50.7
Total	**935**	**537**	**57.4**

Source: GAO Survey of Postsecondary School Experiences with the Direct Loan Program

Estimation

We compared key characteristics of nonrespondents and respondents. We performed an analysis to determine whether there were significant differences between respondents and nonrespondents on several key characteristics. Separately for respondents and nonrespondents, we estimated the percentage of schools that participated in both the Direct Loan Program and FFELP and the proportion of schools participating in the Direct Loan Program for 6, 7, or 8 years. We performed this analysis for all Direct Loan schools, and also separately for each of our strata (school type). For most of the comparisons, these characteristics were not significantly different between the respondents and the nonrespondents. Additionally, we estimated average loan volume and average enrollment for the respondents and the nonrespondents. Although the results of this estimate indicate that respondents have larger loan volume and enrollments for some strata, survey estimates related to loan volume or enrollment are not contained in this report.

Because our sample contained a large proportion of the total population of schools, and because of the result of our comparison of respondent and nonrespondent-based estimates, we chose to include the survey results in our report and to project sample-based estimates for the total population of schools in our study population.

All population estimates based on this survey are for the target population defined as Direct Loan schools. Estimates of this target population were computed using methods that are appropriate for a stratified probability sample. Within each stratum, we formed estimates by weighting the survey data by the ratio of the population size to the sample size. This method of estimation assumes that the response for this survey was equivalent to probability sampling within each stratum.

Sampling and Nonsampling Error

As with all sample surveys, this survey is subject to both sampling and nonsampling errors. The effects of sampling errors, due to the selection of a sample from a larger population, can be expressed as confidence intervals based on statistical theory. Sampling errors occur because we use a sample to draw conclusions about a larger population. As a result, the sample was only one of a large number of samples of schools that might have been obtained from the population of all Direct Loan schools. If a different sample had been taken, the results might have been different. To recognize the possibility that other samples might have yielded other results, we express our confidence in the precision of our particular sample's results as a 95-percent confidence interval. The 95-percent confidence interval is expected to include the actual results for 95 percent of samples of this type. For percentage estimates in this report, we are 95 percent confident that when sampling error is considered, the results we obtained are within +/- 6 percentage points of what we would have obtained if we had surveyed the entire study population, unless otherwise noted. For example, we estimate that 90 percent of the schools reported that streamlined loan process was an extremely or very important factor in influencing the decision to join the Direct Loan Program. The 95-percent confidence interval for this estimate would be no wider than +/-6 percentage points, or from 84 to 96 percent.

In addition to the reported sampling errors, the practical difficulties of conducting any survey introduce other types of errors, commonly referred to as nonsampling errors. For example, questions may be misinterpreted, some people may be less likely than others to respond to the survey, errors could be made in recording the questionnaire responses, or the respondents' opinions may differ from those of financial aid officials at schools that did not respond to our survey. We took several steps to reduce these errors. Prior to fielding the questionnaire, we pretested the data collection instrument with six schools to ensure that respondents would understand the questions and that answers could be provided. Because this was a Web survey, the responses were directly entered by respondents and were not subject to other data entry errors. Data edits and estimation programs were independently verified to ensure that programming errors did not affect our estimates. To reduce nonresponse, we sent two follow-up emails to all schools that had not responded to the survey by our deadline. Additionally, we conducted an intensive follow-up with a randomly selected group of 100 nonrespondents that had participated in the Direct Loan Program in 2001-02 and received responses from an additional 35 schools that were included in our final survey results.

Analysis of Benefits Offered by FFELP Lenders

In order to examine financial benefits available from different FFELP lenders, we obtained information through the Web sites of the eight FFEL lenders with the highest amount of loan originations in fiscal year 2002—each made federal loans of more than a billion dollars—and all 36 guaranty agencies. We also interviewed two FFELP lenders and an organization that represents FFELP lenders.

Site Visits

We conducted interviews with financial aid officials at 20 current Direct Loan schools of various types that were located in the Boston, New York City, San Francisco, and Washington, D.C., metropolitan areas. We selected schools based on school type and loan volume. These schools included 6 public 4-year schools, 6 private 4-year schools, 4 2-year schools, 3 less-than-2-year schools, and 1 public university system that includes 12 4-year and 5 2-year schools.[3] At the time of our visits, 13 of these schools participated only in the Direct Loan Program and 7 participated in both the Direct Loan Program and FFELP. See table 5.

[3]We visited a university official at the City University of New York, because Direct Loan Program operations are centralized for its campuses.

Table 5: Characteristics of Schools Selected for Site Visits and Interviews

Name of school	School type	Student enrollment, fall 1998	Direct Loan volume, 2001-02	FFELP volume, 2001-02
Boston area, located in FSA Region I				
Suffolk University	4-year private	6,445	$15,791,907	$27,789,571
Benjamin Franklin Institute of Technology	4-year public	279	$1,166,773	$0
Harvard University	4-year private	24,373	$77,643,462	$0
New England College of Optometry	4-year private	422	$9,535,668	$0
Porter and Chester Institute	Less-than-2-year	1,072	$5, 421,063	$0
New York City, located in FSA Region II				
City College of New York	4-year and 2-year public	194,746 (total at 17 campuses)	$87,598,773 (total at 17 campuses)	$0
Cornell University Medical College	4-year private	692	$6,966,706	$200,931
Technical Career Institute	2-year private	3,545	$538,731	$6,744,374
New York International Beauty School	Less-than-2-year	168	$528,310	$25,282
DC Metro area, located in FSA Region III				
Bowie State University	4-year public	5,024	$14,789,515	$0
University of Maryland, University College	4-year public	14,142	$44,038,905	$0
Johns Hopkins University	4-year private	17,111	$37,382,682	$4,702,746
Northern Virginia Community College	2-year public	36,216	$1,766,193	$0
RETS Technical Training Center	2-year private	476	$391,581	$2,227,900
Sanz School	Less-than-2-year	611	$1,895,126	$0
San Francisco area, located in FSA Region IX				
San Francisco State University	4-year public	27,446	$57,413,020	$3,817,165
Sonoma State University	4-year public	7,003	$19,346,287	$0
University of California, Berkeley	4-year public	31,011	$92,029,808	$0
University of San Francisco	4-year private	7,990	$46,255,625	$0
Napa Valley College	2-year public	5,646	$348,260	$0

Source: GAO Analysis of Education data.

Telephone Interviews

We also conducted telephone interviews with financial aid officials at two Direct Loan schools—the University of Nebraska and the University of Idaho—and financial aid officials at three former Direct Loan schools—the University of Vermont, Michigan State University, and Indiana University.

Appendix II: Comments from the Department of Education

UNITED STATES DEPARTMENT OF EDUCATION

Federal Student Aid
Chief Operating Officer

November 13, 2003

Ms. Cornelia Ashby
Director, Education, Workforce,
and Income Security Issues
General Accounting Office
Washington, D.C. 20548

Dear Ms. Ashby:

Thank you for the opportunity to respond to your draft audit report entitled, *"Direct Student Loan Program – Management Actions Could Enhance Customer Service"* (GAO-04-107). I am responding on behalf of the Department.

The William D. Ford Federal Direct Loan (Direct Loan) Program has assisted millions of American students each year in attaining their higher education goals. With the introduction of the Direct Loan Program, benefits for borrowers, as well as customer service for schools, improved in both the Direct Loan and Federal Family Education Loan (FFEL) Programs.

The Department continuously seeks to improve delivery of services to borrowers. For example, as noted in your report, the Department implemented a new system, the Common Origination and Disbursement (COD) system that originates and disburses Direct Loans to students faster, but is also aimed at simplifying and improving the reconciliation requirements of the program. We are pleased that you report, based on a survey, that 72 percent of Direct Loan schools are generally satisfied with COD. The Department will continue to find new ways to enhance the user-friendliness of the new system.

While it is true that the Department has not collected information from schools that have stopped participating in the Direct Loan Program, we have supported a continuous program of soliciting information from schools concerning program improvements. Each year, general sessions are offered at our Electronic Access Conferences and at our Spring Conference that invite schools to provide feedback on program operations. In addition, focus groups are held with invited schools as part of the annual system development process. Therefore, we suggest that GAO acknowledge that the Department does provide a forum for program improvement suggestions on a continual basis.

However, the Department concurs with your recommendation that FSA systematically collect information from schools that could be used to make improvements to the Direct Loan Program. In the future, the Department will conduct exit interviews of schools that notify us when they are

Our mission is to ensure equal access to education and to promote educational excellence throughout the nation.

Page 2

leaving the Direct Loan Program. As appropriate, we will incorporate the results into requirements for the annual award year development process.

Again, thank you for the opportunity to comment on this draft report. We appreciate the professionalism of your staff as they worked on this engagement. If you have any questions, please contact Ms. Kay Jacks at (202) 377-4288.

Sincerely,

Theresa S. Shaw

Appendix III: GAO Contacts and Staff Acknowledgments

GAO Contacts

Jeff Appel, Assistant Director (202) 512-9915
Andrea Romich Sykes, Analyst-in-Charge (202) 512-9660

Staff Acknowledgments

In addition to those named above, the following people made significant contributions to this report: Carla Craddock, Kathleen White, Margaret Armen, Cynthia Decker, Luann Moy, Mimi Nguyen, Mark Ramage, Bonita Vines, and Weili Shaw.

GAO's Mission

The General Accounting Office, the audit, evaluation and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through the Internet. GAO's Web site (www.gao.gov) contains abstracts and full-text files of current reports and testimony and an expanding archive of older products. The Web site features a search engine to help you locate documents using key words and phrases. You can print these documents in their entirety, including charts and other graphics.

Each day, GAO issues a list of newly released reports, testimony, and correspondence. GAO posts this list, known as "Today's Reports," on its Web site daily. The list contains links to the full-text document files. To have GAO e-mail this list to you every afternoon, go to www.gao.gov and select "Subscribe to e-mail alerts" under the "Order GAO Products" heading.

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are $2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. General Accounting Office
441 G Street NW, Room LM
Washington, D.C. 20548

To order by Phone:	Voice:	(202) 512-6000
	TDD:	(202) 512-2537
	Fax:	(202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Public Affairs

Jeff Nelligan, Managing Director, NelliganJ@gao.gov (202) 512-4800
U.S. General Accounting Office, 441 G Street NW, Room 7149
Washington, D.C. 20548

PRINTED ON RECYCLED PAPER