SESSION 24

Overview of the William D. Ford Federal Direct Loan Program and the Federal Family Education Loan Program

Instructor's Notes

Time Estimate:
Lecture 45 minutes
Exercise 15 minutes
Total Time: 60 minutes

By the end of this session, you will be able to:

- *identify similarities and differences between the two loan programs,*
- *calculate loan eligibility for subsidized, unsubsidized, and PLUS Loans, and*
- *determine when loan proration is required.*

INTRODUCTION

This session offers an overview of the William D. Ford Federal Direct Loan Program (Direct Loan Program) and the Federal Family Education Loan (FFEL) Program. In combination, they annually provide over 20 billion dollars in loans to students and their parents.

While these programs share many similarities, they also have some important distinctions. In the Direct Loan Program, now in its fourth year of operation, students and parents borrow directly from the U.S. Department of Education (ED). In the FFEL program, banks and other private lenders serve as the source of funds. To emphasize the similarities and differences, we've divided this session into two parts.

- The first part provides general information that applies to both the Direct Loan and FFEL Programs.
- The second part highlights the differences between the programs.

Instructor's Notes

GENERAL INFORMATION ABOUT THE DIRECT LOAN AND FFEL PROGRAMS

The Direct Loan Program and the FFEL Program have a number of components in common, including: (OH 1)

1

- the types of loans available,
- how loan amounts are calculated,
- the amounts of loan fees and interest charged,
- loan counseling requirements, and
- certain repayment provisions.

Loan Types

The Direct Loan Program and the FFEL Program consist of four types of loans: (OH 2)

2

- Subsidized loans, for students enrolled at least half time;
- Unsubsidized loans, for students enrolled at least half time;
- PLUS Loans, for parents of dependent undergraduate students; and
- Consolidation Loans, for student or parent borrowers, to combine existing federal education loans into a new, single loan.

Q: What is the difference between a subsidized and an unsubsidized loan?

A: With a subsidized loan, ED covers the interest for the borrower during periods of at least half-time enrollment, grace, and deferment. Unsubsidized means that the borrower is responsible for paying all the interest throughout the life of the loan. PLUS Loans are always unsubsidized.

Instructor's Notes

Loan Limits and Calculations

Subsidized and unsubsidized loans have both annual and aggregate loan limits. Annual limits are yearly maximums, while aggregate limits are cumulative limits for a student's entire undergraduate and graduate career. Overall, these limits are based on a student's grade level, year of study, and financial need. Turn to the loan limits chart on page 3 of your Workbook. [IG, pg. 16]

PW 3

The chart differentiates between base and additional loan amounts.

- The **base amount,** made up of both subsidized and unsubsidized loans, is the initial loan limit for all student borrowers. (OH 3)

  3

  - The amount of subsidized funds that make up the base amount depends on the student's need.

- The **additional amount** may be borrowed on top of the base amount by all independent students, and by dependent students whose parents are unable to borrow PLUS Loans because of a poor credit history. (OH 4)

  4

  - Remember, financial aid administrators can declare dependent students to be independent students because of exceptional circumstances. A dependency override must be clearly documented in the student's file.

Calculating a student's base and additional amounts requires a financial aid administrator to consider various elements we have talked about in previous sessions, including cost of attendance (COA), Expected Family Contribution (EFC), and estimated financial assistance (EFA). EFA includes **all** of a student's financial aid, including nonfederal aid, such as private scholarships.

Instructor's Notes

Base Amounts

The top half of the chart deals with base amounts. Keep in mind that these are maximums; the total any individual student can actually borrow is determined by COA, EFC, and EFA.

The subsidized base amount a student may borrow is always calculated first. The equation is as follows: (OH 5)

5

COA
- EFC
- EFA

= Eligibility for subsidized loan

Calculating the unsubsidized base amount is similar, but you only consider COA and EFA, not EFC. The EFA now must include the subsidized loan for which the student is eligible. The equation is: (OH 6)

6

COA
- EFA (including the subsidized loan)

= Eligibility for unsubsidized loan

Remember, though, a student may not receive more than the loan limit prescribes.

Let's calculate the subsidized and unsubsidized base amounts for a sample student. Take a look at Tonya's situation, on page 9 of your Workbook. ***PW 9***

Tonya is a dependent, second-year student. She has a COA of $5,530. Her EFC is $1,750. The only financial aid she is scheduled to receive so far is a $1,250 Pell Grant. Take a few minutes to calculate Tonya's base loan amounts.

Q: What is Tonya's EFA?

A: $1,250. Her Pell Grant is the only EFA component.

Instructor's Notes

Q: What is her subsidized base amount?

A: $2,530. You get this amount by subtracting her EFC and EFA from her COA. This is the total subsidized loan amount for which Tonya is eligible. (OH 7)

7

Q: What is Tonya's initial base unsubsidized loan amount?

A: $1,750. First you include her subsidized amount of $2,530 in her EFA. Then you subtract her new EFA of $3,780 from her COA. (OH 8)

8

We have a problem, though. Tonya's loan limit is $3,500. If you certified a subsidized loan for $2,530 and an unsubsidized loan for $1,750, you would exceed the $3,500 limit.

Q: Therefore, what is the actual unsubsidized loan amount Tonya can receive?

A: $970. To get this, you subtract the subsidized base amount from the loan limit of $3,500. (OH 9)

9

Any questions about determining a student's base amount?

Additional Amount

The bottom half of the loan chart deals with additional loan amounts. Independent students and dependent students whose parents are unable to borrow PLUS Loans are eligible for this amount, as long as their costs of attendance haven't already been met by the base amount.

PW 3

- Note that students whose parents **refuse** to borrow PLUS Loans are **not** eligible for the additional amount. Only students whose parents try to borrow a PLUS Loan but are not approved because of an adverse credit history can get the additional amount.

Instructor's Notes

10

Calculating a student's additional loan amount again involves COA and EFA. Expected Family Contribution is not a factor, as the additional amount is always unsubsidized. The equation is: (OH 10)

	COA
-	EFA (including base amount)
=	Eligibility for additional amount

The EFA now includes the entire base loan amount, along with the other student aid.

Let's continue with Tonya, on page 10 of your Workbook. ***PW 10***

Tonya's parents are denied a PLUS Loan. Therefore, Tonya is eligible for additional unsubsidized loan money. Calculate Tonya's additional eligibility.

Q: What is the additional amount Tonya can borrow?

A: $780. Her EFA, now $4,750, is subtracted from the COA of $5,530. Since $780 is well below the limit of $4,000, Tonya can get the full amount she needs to meet her COA. (OH 11)

11

What questions do you have?

We haven't mentioned loan limits for parent loans. The reason: PLUS Loans actually have no limit. You simply subtract the EFA from the COA. If Tonya's parents were eligible, they could have borrowed the $780 for their daughter.

Q: If they didn't want Tonya to borrow anything at all, how much PLUS would they need? Remember, Tonya will still get her $1,250 Pell Grant.

A: $4,280. That's her COA ($5,530) minus her EFA ($1,250). (OH 12)

12

Any questions?

Instructor's Notes

Proration

Undergraduates are not always eligible for the maximum loan limits. There are two situations that require a school to **prorate**, or calculate a percentage of the loan limit, thereby creating a lower maximum amount.

Proration is required when:

- the student's entire program is less than one academic year

  OR

- the student's program is greater than an academic year, but the student's final period of enrollment is less than an academic year.
  - For term-based schools, the remainder of a program is considered shorter than an academic year when it contains fewer terms than the school's academic year.

With this in mind, let's look at some examples. Please turn to page 11 of your Workbook. ***PW 11***

In Exercise 1, Michael is enrolled in a computer-training program that is 600 clock hours and 15 weeks long.

The academic year is defined as 900 clock hours and 30 weeks.

Q: Is proration required here for Michael?

A: Yes. Michael's entire program is less than an academic year in length.

Now let's look at Exercise 2. Charlene is beginning her second year. Her school's academic year contains two semesters. Each semester is 15 weeks long. Because she enrolled during the summer, she only has 18 credits left to take. She will take them during the fall semester to complete her program in December.

Instructor's Notes

Q: Is proration required for Charlene? Why or why not?

A: Yes. Her final period of enrollment is only one term, which is shorter than her school's two-term academic year.

In Exercise 3, Charlene's plans change, and she will take 6 credits in the fall semester and 12 credits in the spring semester, graduating in May.

Q: Is proration still required for Charlene?

A: No, because her final period of enrollment is a full academic year; she is attending both semesters in the school's academic year. Note that the number of credits Charlene takes is irrelevant when discussing proration. All that matters is that she is attending both semesters.

Once you determine the need for proration, the chart on page 4 of your Workbook is used to calculate the new loan limits. Please turn to that chart now. [IG, pg. 17] *PW 4*

Notice that as the length of the student's program or final period of enrollment decreases, as listed in the first column, the student's loan maximums decrease.

Also note the fractions used for both fixed and proportional proration. While we will not delve further into proration now, we have included an appendix to this session that contains explanations, worksheets, and case studies. Please take time later to work through the material.

Loan Fees and Interest

When talking to students about how much they can borrow, schools should remind them that the loan proceeds they actually receive are less than the total amount borrowed. The reason is that borrowers are responsible for paying loan fees. Generally, the fees are collected by deducting them from the loan amount. (OH 13) 13

Instructor's Notes

- There is a 4% loan fee deducted from the proceeds of a borrower's Direct Loans.
- FFEL lenders may charge a borrower a maximum origination fee of 3%. An insurance premium of up to 1%, which may be charged by a guaranty agency to a lender, may be passed on to the borrower. In total, then, up to 4% can be deducted from a borrower's FFEL Program loan.

Let's look at interest on the loan, another cost to the borrower.

Please turn to page 5 of your Workbook and look at the chart, "Direct Loan Program and FFEL Program Interest-Rate Provisions." [IG, pg. 18]

PW 5

Take a moment to study the chart.

Q: What is the current maximum annual interest rate for subsidized and unsubsidized loans and PLUS Loans?

A: On subsidized and unsubsidized loans, the interest rate is variable, not to exceed 8.25%. For PLUS Loans, the interest rate is variable, not to exceed 9%.

The current interest rate for a subsidized or unsubsidized loan first disbursed on or after July 1, 1997 is 7.66%. A PLUS Loan first disbursed on or after July 1, 1997 will have an interest rate of 8.72%.

Note to Instructor: Interest rates for the 1998-99 year were not available when this material went to print.

Certain Repayment Provisions

Grace Period

Now take a moment to look at the chart on page 6 of your Workbook. It describes the grace-period provisions for the Direct Loan and FFEL Programs. [IG, pg. 19]

PW 6

Instructor's Notes

The **grace period** is a period of time during which the student is not responsible for making payments. It begins when the student ceases to be enrolled at least half time, and it lasts for six months. For subsidized loans, interest is covered by the federal government. However, for unsubsidized loans, interest continues to accrue.

- PLUS Loans have no grace period. Interest begins to accrue on the date of the loan's first disbursement. The repayment period begins on the date the loan is fully disbursed.

Deferment and Forbearance

Deferment or **forbearance,** which are temporary cessations of payment, may be obtained for a variety of reasons, such as enrollment at least half time at an eligible school **or** economic hardship.

Deferment and forbearance are available for the life of a loan, within certain limits. They are granted in intervals of several months, and borrowers assume the responsibility of renewing them if their situation has not changed.

Note to Instructor: Generally, there are no time limits on forbearances other than they may be granted for up to one year (12 months) at a time. Many deferments have a 3-year limit.

As it does during a grace period, the federal government will cover interest for subsidized loans during any period of deferment. Interest will not be covered during any period of deferment of an unsubsidized loan, or during a forbearance of either type of loan. A student may pay the interest as it accrues, or allow it to be capitalized at the end of the period of deferment or forbearance.

PLUS borrowers are also eligible for certain deferments and forbearance. For example, parents who borrowed PLUS Loans and are themselves full-time students may obtain deferments.

For more information on grace periods, deferments, and forbearance, refer to Chapters 10 and 11 in the Handbook.

Instructor's Notes

Cancellation and Loan Forgiveness

Take a look at the chart titled "Cancellation and Loan Forgiveness" on page 7 of your Workbook. [IG, pg. 20]

PW 7

Counseling Students

With the increasing availability and use of student loans—and related concern about defaults—the school's role in loan counseling is critical.

- Schools must conduct entrance loan counseling for all first-time student borrowers under the Direct Loan and FFEL Programs.
  - PLUS Loan borrowers do not have to undergo loan counseling.
- Schools must also conduct exit loan counseling under both loan programs.
  - Transfer students who previously received Direct Loan or FFEL funds do not have to undergo entrance loan counseling, but still must undergo exit loan counseling.

Take a moment to read the chart on page 8 of your Workbook, which summarizes the "How," "When," and "What" of loan counseling for both loan programs. [IG, pg. 21]

PW 8

Instructor's Notes

Remember, you must document in each student's file that the entrance counseling requirements have been fulfilled.

During the entrance loan counseling, the financial administrator should also: (OH 14)

14

- cover all sources of financial aid and emphasize the constraints on various aid sources;
- urge students to read and save all loan documents;
- review the school's requirements for satisfactory academic progress;
- inform students to borrow only the amount needed to meet their educational expenses; (OH 15)

15

- review the school's refund policy; and
- review the students' loan rights and responsibilities.

One of the features of exit counseling is to check for errors in the school records regarding the student's name, address, Social Security number, and other vital student data.

- Within 60 days of the exit counseling, the school must report any corrections to this information to ED (for Direct Loans) or the appropriate guaranty agency (for FFEL funds). (OH 16)

16

As with entrance counseling, the school must document in the borrower's file that it has provided the required exit counseling.

Schools with high student-loan default rates may be required to provide extra loan counseling. Upon review of the school's default reduction plan, ED may require them to provide additional counseling to students.

- Schools with default rates that exceed ED's mandatory thresholds will be terminated from the Direct Loan and FFEL Programs.
- For more details, study Chapters 10 and 11 of the Handbook. This chapter addresses default reduction measures.

Any questions about the similarities between the programs?

DIFFERENCES BETWEEN DIRECT AND FFEL

Now let's look at the major differences in the two programs.

Source of Funds

The basic difference between Direct Loans and Federal Family Education Loans is the source of funds.

Q: What is the source of Direct Loan funds?

A: The federal government, through the U.S. Department of Education.

FFEL funds, on the other hand, come from private lenders. However, because the loans are unsecured, these lenders are backed by state guaranty agencies (GAs). The guaranty agencies often purchase the loans from the lenders. Backing the GAs is the federal government. When GAs are unable to collect defaulted student loans, they subrogate the loans to ED.

The Application Process

Another difference is the application process. While borrowers must complete the FAFSA to apply for either a

Instructor's Notes

Note to Instructor: Subrogation involves ED compensating the GAs for defaulted student loans, and then collecting the amount due from the students.

Instructor's Notes

Direct Loan or Federal Family Education Loan, an additional application is required of FFEL borrowers. In Session 25, we'll take a closer look at the FFEL application.

Repayment

The repayment process differs as well. Because Direct Loans come directly from ED, the borrower only has ED to repay. FFEL borrowers may have to repay a number of lenders, guaranty agencies, or other loan holders.

The repayment options also differ.

Direct Loan borrowers have four options: (OH 17)

17

- standard repayment,
- extended repayment,
- graduated repayment, and
- income-contingent repayment.

FFEL, on the other hand, offers standard, graduated, and income-sensitive repayment. (OH 18)

18

Borrowers choose the plan that best suits them.

Both programs offer Consolidation Loans. However, the terms are different in the two programs.

- Differences include interest rates and repayment options.

Do you have any final questions? Now it's time for the final exam. Complete the True/False quiz on page 12 of your Workbook. [IG, pg. 15]

PW 12

» Give participants a few minutes to complete the quiz. Then take any questions

BACK AT THE OFFICE

PW 13

What should you do when you return to your office?

Instructor's Notes

Review Quiz — True or False

Directions: Place a "T" or "F" after each statement.

1. An undergraduate student's loan must be prorated if her final period of study is one academic year or greater in length. **F**
2. ED will cover the interest during any period of deferment or forbearance for a subsidized loan. **F**
3. For the unsubsidized portion of a student's base amount, EFC is not considered. **T**
4. To compensate for interest fees, a borrower's Direct Loan will actually be set at 4% higher than the amount for which the borrower is eligible. **F**
5. Both Direct Loans and FFELs require an additional application besides the FAFSA. **F**
6. 7. PLUS loans can only be calculated after the student's base loan amount has been determined. **F**
8. All independent students are eligible for the additional unsubsidized loan amount as long as their COA has not been met. **T**
9. The Direct Loan grace period is a few months longer than the FFEL grace period. **F**
10. Both base and additional loan amounts may consist of a combination of subsidized and unsubsidized loans. **F**

LOAN LIMITS: DIRECT AND FFEL

BASE - SUBSIDIZED & UNSUBSIDIZED

STUDENT YEAR	ANNUAL	CUMULATIVE
1st-year undergrad.	$2,625	
2nd-year undergrad.	$3,500	
3rd, 4th, 5th-year undergrad.	$5,500	$23,000
graduate student	$8,500	$65,500 (includes undergrad. & graduate total)

ADDITIONAL - UNSUBSIDIZED ONLY

STUDENT YEAR	ANNUAL	CUMULATIVE
1st-year undergrad.	$4,000	
2nd-year undergrad.	$4,000	
3rd, 4th, 5th-year undergrad.	$5,000	$23,000 (Dependent) $46,000 (Independent)
graduate student	$10,000	$138,500 (includes undergrad. & graduate sub. and unsub. total)

LOAN PRORATION: DIRECT LOAN AND FFEL PROGRAMS

Program Length or Final Enrollment Period	Grade Level					
	First-Year Undergraduate		Second-Year Undergraduate		Third-Year, Fourth-Year, and Fifth-Year Undergraduate	
	Base Stafford (sub and unsub)	Additional Unsub Stafford	Base Stafford (sub and unsub)	Additional Unsub Stafford	Base Stafford (sub and unsub)	Additional Unsub Stafford
1 academic year	$2,625	$4,000	$3,500	$4,000	$5,500	$5,000
Less than 1 and greater than or equal to 2/3 academic year	$1,750	$2,500	Proportional Proration	$2,500	Proportional Proration	Proportional Proration
Less than 2/3 and greater than or equal to 1/3 academic year	$875	$1,500	Proportional Proration	$1,500	Proportional Proration	Proportional Proration
Less than 1/3 academic year	0	0	Proportional Proration	0	Proportional Proration	Proportional Proration

Calculation Notes:

- Pre-set loan amounts represent **fixed proration**. To prorate, take the lesser of the two fractions (see below), find the appropriate box in the first column that matches your fraction, and find the dollar amount that represents your new loan maximum in the appropriate grade level column.

Compare $\frac{\text{clock/credit hours in program}}{\text{clock/credit hours in the schools}}$ and $\frac{\text{\# of weeks in program}}{\text{\# of weeks in academic year}}$

academic year

- For proportional proration, simply multiply the regular maximum with the fraction below. You can ignore the first column altogether when doing proportional proration.

Use $\frac{\text{\# credit/clock hours left in the program}}{\text{\# credit/clock hours in schools academic year}}$

Direct Loan Program and FFEL Program Interest-Rate Provisions as of July 1, 1994

	Subsidized and Unsubsidized Loans	PLUS Loans
Interest Rate	Variable rate; maximum annual rate 8.25%	Variable rate; maximum annual rate 9%
Interest Rate Formula	***For loans first disbursed on or after 07/01/94 through 06/30/95:*** • Bond equivalent rate of 91-day Treasury bills auctioned at final auction prior to 06/01 plus 3.1% ***For loans first disbursed on or after 07/01/95 through 06/30/98:*** • **Prior to repayment,** bond equivalent rate of 91-day Treasury bills auctioned at final auction prior to 06/01 plus 2.5% • If borrower is **in repayment,** bond equivalent rate of 91-day Treasury bills auctioned at final auction prior to 06/01 plus 3.1%	***For loans first disbursed on or after 07/01/94 through 06/30/98:*** • Bond equivalent rate of 52-week Treasury bills auctioned at final auction prior to 06/01 plus 3.1%

Grace Periods for Direct Loan Program and FFEL Program

Federal (Subsidized) Stafford Loan[1] and Direct Subsidized Loan[1]	Federal Unsubsidized Loan[2] and Direct Unsubsidized Loan	Federal PLUS Loan and SLS[2,3] and Direct PLUS Loan
6 months for all loans for periods of enrollment 01/01/81 and after.[5] 9-12 months for all loans for periods of enrollment before 01/01/81.	6 months on repaying principal. Interest may be paid or accrued and capitalized during in-school and grace periods.[4]	None. The repayment period begins on the date the loan is fully disbursed. Interest begins to accrue on the date of the loan's first disbursement. For Federal SLS borrowers and new borrowers of Federal PLUS Loans on or after 07/01/93, repayment may be deferred while the students for whom the funds are borrowed are enrolled at least half time. Interest may be capitalized.

[1] If the grace period has not already been used, the loan's grace period begins on the date the student ceases to be enrolled at least half time.
[2] Also applied to Federal SLS loans, which were discontinued 07/01/94.
[3] Combined Federal SLS/federal sub/unsub borrowers have the option to defer Federal SLS repayment for up to 6 months after at least half-time enrollment ceases. This provision applies only when the borrower's loans have not entered repayment.
[4] Paying accrued interest is postponed by adding it to the loan principal as the interest comes due. (This is called "capitalization.")
[5] Not all loans made after 1/1/81 have 6 months grace period. If a student received a 7% loan prior to 1/1/81 with a 9-12 month grace period, the student continued to receive the 7% interest rate and the 9-12 month grace period on subsequent loans up until 7/1/94. Beginning 7/1/94 all loans had variable interest rates and 6 months grace period.

Cancellation and Loan Forgiveness

Borrower	Direct and FFEL Loans
Loan Cancellation	• death of borrower • death of student on whose behalf a parent borrowed a PLUS Loan • permanent and total disability of borrower • discharge of loan in bankruptcy
Loan Forgiveness	• students unable to complete their programs of study because their schools closed[1] • students whose schools falsely certified their loans

[1]These students are only eligible for forgiveness if their schools do not provide them with an alternate way to complete their program. This may include attendance at another nearby school that has an agreement in place with the closing school.

Entrance/Exit Loan Counseling For Direct Loans and FFEL Programs Loans

HOW to cover:	
ENTRANCE COUNSELING ◊ In-person presentation or by videotape or by computer-assisted technology. Individual with Title IV expertise must be available to answer borrower questions ◊ Written counseling materials permissible for students enrolled in correspondence study or study-abroad programs *OR* ◊ "Alternative Entrance Counseling Approach" for Direct Loan borrowers only: • Written counseling material provided to first-time Direct Loan borrowers • Counseling efforts targeted to certain groups of borrowers • Entrance-counseling plan must be part of school's quality assurance plan	**EXIT COUNSELING** ◊ In-person presentation ◊ Written counseling materials: • Mandatory for students who have withdrawn without notifying the school or have failed to attend scheduled exit counseling • Permissible for students enrolled in correspondence study or study-abroad program
WHEN to cover:	
ENTRANCE COUNSELING ◊ Prior to delivery of the first disbursement of the first Stafford Loan a borrower will receive at your school.	**EXIT COUNSELING** ◊ Shortly before any borrower ceases at least half-time enrollment or (by mail) within 30 days: • After learning that the student has withdrawn without the notifying school • After the student has failed to attend scheduled exit counseling • After student completed correspondence program or study-abroad program
WHAT to cover:	
REQUIRED CORE ITEMS	
ENTRANCE COUNSELING ◊ Emphasize seriousness and importance of repayment ◊ Emphasize consequences of default, including adverse credit reports, garnishment of wages, and litigation ◊ Emphasize obligation to repay full amount of loan, regardless of borrower's ability to gain employment after leaving school or dissatisfaction with the program ◊ For Direct Loans, provide data on average indebtedness and average monthly repayment of students who obtained loans at that school or in borrower's program of study	**EXIT COUNSELING** ◊ Provide name and address of the borrower's lender(s) ◊ Inform student of average monthly repayment amount based on student's indebtedness ◊ Review available repayment options & obligations ◊ Provide borrower with debt-management strategies that would facilitate repayment ◊ Explain how to contact the party servicing the student's loan ◊ Emphasize seriousness and importance of repayment ◊ Emphasize consequences of default, including adverse credit reports, garnishment of wages, and litigation ◊ Review deferment, forbearance, and cancellation conditions ◊ Require borrower to provide corrections to school's records concerning name, address, Social Security number, references, driver's license number with state where it was issued, and name and address of expected employer