

Department of Education
STUDENT LOANS OVERVIEW
Fiscal Year 2009 Budget Request

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DEPARTMENT OF EDUCATION FISCAL YEAR 2009 PRESIDENT'S REQUEST

Office, Account, Program and Activity	Category Code	2007 Annual CR Operating Plan	2008 Appropriation	2009 President's Request	Change from 2008 Appropriation	
					Amount	Percent
Federal Direct Student Loans Program Account (HEA IV-D)						
1. New loan subsidies (HEA IV-D)	M	264,613	255,559	328,670	73,111	28.6%
2. Upward reestimate of existing loans	M	4,702,101	1,158,458	0	(1,158,458)	-100.0%
3. Upward modification of existing loans	M	0	4,143,273	0	(4,143,273)	-100.0%
4. Downward reestimate of existing loans (non-add)	M	(984,538)	(573,939)	0	573,939	-100.0%
5. Downward modification of existing loans (non-add)	M	0	0	(1,591,034)	(1,591,034)	---
6. Net reestimate of existing loans (non-add)	M	3,717,563	584,519	0	(584,519)	-100.0%
7. Net modification of existing loans (non-add)	M	0	4,143,273	(1,591,034)	(5,734,307)	-138.4%
Subtotal, loan subsidies		4,966,714	5,557,290	328,670	(5,228,620)	-94.1%
Subtotal, new loan subsidies and net reestimate/modification (non-add)		3,982,176	4,983,351	(1,262,364)	(6,245,715)	-125.3%
8. Federal administration (HEA IV-D section 458)	M	0	(25,000)	0	25,000	-100.0%
8. Federal administration (HEA IV-D section 458):						
(a) Federal administration	M	0	0	0	0	---
(b) Payments for services to guaranty agencies	M	0	0	0	0	---
Subtotal		0	0	0	0	---
Total	M	4,966,714	5,532,290	328,670	(5,203,620)	-94.1%
<i>Outlays</i>		5,391,146	5,609,564	346,002	(5,263,562)	-93.8%
<i>Federal administration</i>	D	212,688	52,274	17,332	(34,942)	-66.8%
<i>Loan program--mandatory</i>	M	5,178,458	5,557,290	328,670	(5,228,620)	-94.1%
Federal Family Education Loans Program Account (HEA IV-B)						
1. New loan subsidies (HEA IV-B)	M	6,850,098	1,076,427	2,407,263	1,330,836	123.6%
2. Upward reestimate of existing loans	M	555,015	3,446,178	0	(3,446,178)	-100.0%
3. Upward modification of existing loans	M	0	10,835	0	(10,835)	-100.0%
4. Downward reestimate of existing loans (non-add)	M	(3,714,626)	(2,456,227)	0	2,456,227	-100.0%
5. Downward modification of existing loans (non-add)	M	0	(2,475,184)	0	2,475,184	-100.0%
6. Net reestimate of existing loans (non-add)	M	(3,159,611)	989,951	0	(989,951)	-100.0%
7. Net modification of existing loans (non-add)	M	0	(2,464,349)	0	2,464,349	-100.0%
Total, FFEL Program Account	M	7,405,113	4,533,440	2,407,263	(2,126,177)	-46.9%
Total, new loan subsidies and net reestimate/modification (non-add)		3,690,487	(397,971)	2,407,263	2,805,234	-704.9%
<i>Outlays</i>	M	6,934,811	4,698,552	1,817,457	(2,881,095)	-61.3%
Federal Family Education Loans Liquidating Account (HEA IV-B)						
1. Pre-1992 student loans	M	(491,770)	(615,033)	(553,095)	61,938	-10.1%
<i>Outlays</i>	M	(661,436)	(615,033)	(553,095)	61,938	-10.1%
Federal Student Loan Reserve Fund						
1. Capital transfer to Treasury	M	(254,000)	0	0	0	---
<i>Outlays</i>	M	(792,832)	(142,000)	(169,603)	(27,603)	19.4%

NOTES: Category Codes are as follows: D = discretionary program; M = mandatory program.
FY 2008 detail may not add to totals due to rounding.

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Federal Family Education Loan Program (FFEL)

(Higher Education Act of 1965, Title IV, Part B)

William D. Ford Federal Direct Loan Program (Direct Loans)

(Higher Education Act of 1965, Title IV, Part D)

FY 2009 Authorization (\$000s): Indefinite¹

Budget Authority (\$000s):

Net Loan Subsidies:	<u>2008</u>	<u>2009</u>	<u>Change</u>
FFEL New Loan Subsidy ²	\$1,076,427	\$2,407,263	+\$1,330,836
FFEL Net Reestimate ³	989,951	N/A	-989,951
FFEL Net Modification ⁴	-2,464,349	N/A	+2,464,349
FFEL Total Net Subsidy ⁵	-397,971	2,407,263	+2,805,234
Direct Loans New Loan Subsidy ²	255,559	328,670	+73,111
Direct Loans Net Reestimate ³	584,519	N/A	-584,519
Direct Loans Net Modification ⁴	4,143,273	-1,591,034	-5,734,307
Direct Loans Total Net Subsidy ⁵	4,983,351	-1,262,364	-6,245,715

¹ The Higher Education Act (HEA) was extended to March 31, 2008 by the Third Higher Education Extension Act of 2007 (P.L. 110-109). Selected reauthorizing language authorizing the loan programs beyond FY 2008 was contained in the Higher Education Reconciliation Act (HERA) of 2005 (P.L. 109-171). The College Cost Reduction and Access Act (CCRAA) (P.L. 110-84) also amended loan program provisions and other HEA programs effective October 1, 2007. Other reauthorization bills may still be introduced.

² Federal administration funds associated with the FFEL and Direct Loan accounts are shown in **Student Aid Administration**, beginning on page Z-1. FFEL and Direct Loan new loan subsidy reflects the estimated cost of loans to be executed for the 2008 and 2009 cohorts.

³ The net upward reestimates related to costs of outstanding FFEL and Direct Loans reflect the upward reestimates shown in the budget program accounts as well as the downward reestimates shown in the downward reestimate receipt accounts.

⁴ The net downward modification for FFEL in 2008 reflects enactment of CCRAA reducing lender exceptional performance and guaranty agency account maintenance fees and retention. The net upward modification in Direct Loans in FY 2008 also reflects CCRAA provisions creating a new income based repayment plan and new public service loan forgiveness program.

⁵ This total net subsidy provides a net cost of the loan programs taking into account both upward and downward impacts of reestimates and modifications, consistent with the presentation on page Q-1.

PROGRAM DESCRIPTION

The Federal Family Education Loan (FFEL) and William D. Ford Federal Direct Loan (Direct Loan) programs provide students and their families with loans to help meet postsecondary education costs. Non-consolidation FFEL and Direct Loan (net commitment) volume which reflects new student loan demand, continues a strong expansion, more than doubling from \$29 billion in FY 1997 to over \$64 billion in FY 2007. In FY 2007, new loan volume (excluding Consolidations) in both FFEL and Direct Loans accounted for about 78 percent of all new

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

postsecondary aid available from the Department. Consolidation Loan volume, which represents loans issued to pay off existing student loans, grew at a tremendous pace over the past 5 years, particularly in FFEL. Since FY 1994, total FFEL and Direct Loan Consolidation loan volume increased from approximately \$2 billion to an all-time high of almost \$92 billion in FY 2006 and then decreased to about \$50 billion in FY 2007.

The FFEL and Direct Loan programs meet an important Administration strategic goal of helping to ensure the affordability, accessibility, and accountability of higher education, and better prepare students and adults for employment and future learning. Competition between the two programs, and among FFEL lenders, has resulted in better customer service to students and institutions, along with a greater emphasis on efficiency and borrower satisfaction.

The Higher Education Reconciliation Act (HERA) of 2005 (P.L. 109-171), signed into law on February 8, 2006, and the College Cost Reduction and Access Act (CCRAA) (P.L. 110-84), which became law on September 27, 2007, made substantial changes to the FFEL and Direct Loan programs. Many of the changes are discussed within the following program descriptions; budget amounts for 2008 and 2009 reflect enactment of both HERA and CCRAA.

Federal Family Education Loan Program

The FFEL program offers federally guaranteed loans for postsecondary education through private lenders, providing more student aid funding than any other student financial assistance program. Through this program, the Federal Government helps millions of students and their parents finance attendance at over 6,200 participating universities, colleges, and vocational schools by supporting the availability of loans from approximately 3,100 participating banks and other eligible lenders. Under the CCRAA the Federal Government continues to insure lenders against borrower default at the guaranteed rate of 97 percent, but would reduce the lender insurance rate to 95 percent starting in 2013.

The interest rate on new Stafford and Unsubsidized Stafford Loans starting July 1, 2006 is fixed at 6.8 percent. The CCRAA authorized phased reductions to the interest rate for Subsidized Stafford loans borrowed by undergraduates with the rate cut in half to 3.4 percent on July 1, 2011. The interest rate reverts to 6.8 percent as of July 1, 2012. The interest rate on new FFEL PLUS loans starting July 1, 2006 is fixed at 8.5 percent. Under HERA, Stafford borrower origination fees are reduced by 1 percentage point as of July 1, 2006, and further reduced each year until, as of July 1, 2010, fees would be eliminated in the FFEL program. The fee decreased from 2 percent to 1.5 percent on all new Subsidized and Unsubsidized Stafford loans—excluding Consolidation Loans which have no borrower origination fee—as of July 1, 2007. Lenders may pay part or all of this fee on behalf of students. PLUS loans continue to retain a 3 percent borrower origination fee. While HERA reduced borrower origination fees, CCRAA increased lender origination fees from 0.5 percent to 1 percent of the principal loan amount for all FFEL lenders for new loans as of October 1, 2007.

FFEL borrowers may choose from a number of repayment plans including standard, graduated, income-sensitive, and extended. Students may defer payments for various circumstances such as being in school, economic hardship, or active military service. Interest accrues during deferment periods and is capitalized following the end of deferment, except for Subsidized Stafford Loans where the Federal Government pays the interest during periods of authorized deferment.

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FFEL and Direct Loans

The CCRAA added a new income-based repayment plan that is available to both FFEL and Direct Loan borrowers who are considered to be in a “partial financial hardship” based on their annual repayment amount in relation to their adjusted gross income. Generally, a borrower would not have to repay on a monthly basis more than 15 percent of their discretionary income or 15 percent of the amount by which the borrower’s adjusted gross income exceeded 150 percent of the poverty line, divided by 12. Any outstanding balance would be forgiven after 25 years of repayment in the income-based repayment option. All plans except the income-based and extended FFEL repayment plans have 10-year repayment terms. The extended plan allows up to 25 years for repayment. Borrowers may change plans once per year.

In the FFEL program, 35 State and private nonprofit guaranty agencies perform loan processing and maintenance services on behalf of FFEL lenders and the Federal Government. These agencies provide training and guidance to participating lenders and schools to ensure compliance with program regulations and assist students with appropriate financial arrangements in order to prevent students from defaulting on their student loans. Under HERA, for new guaranteed loans made after July 1, 2006, guaranty agencies are required to charge borrowers a default fee equal to 1 percent of loan principal; these fees are then deposited into the Student Loan Reserve Fund. Previously, the collection of this fee—referred to as an insurance premium—was optional.

Guaranty agencies also collect on defaulted loans on which they have paid claims to lenders. Borrowers may be charged for these collection costs. Under CCRAA, as of October 1, 2007, the guaranty agency retention rate was reduced from 23 to 16 percent with the balance returned to the Federal Treasury. Under HERA, as of October 1, 2006, guaranty agencies are required to charge borrowers collection costs of not more than 18.5 percent of the outstanding principal and interest on defaulted loans paid off through consolidation; of this amount, 8.5 percent would be remitted to the Government. Effective October 1, 2009, guaranty agencies will be required to remit the entire 18.5 percent collection cost to the Government for any default collections made through consolidation that exceed 45 percent of the guaranty agency’s total collections.

New FFEL loan volume was \$51.3 billion in FY 2007, accounting for about 80 percent of all new FFEL and Direct Loan (non-consolidation) student loan volume. New FFEL loan volume (excluding Consolidations) is projected to increase to \$59.3 billion in the 2009 budget year. (See New Student Loan Volume table, pg. Q-13.) Across the entire FFEL program—including the Liquidating account with loans issued before 1992—there were approximately \$385 billion in FFEL loans outstanding at the end of FY 2007.

William D. Ford Federal Direct Loan Program

The Direct Loan program assists student and parent borrowers by providing loans directly from the Federal Government. Under Direct Loans, the Federal Government provides loan capital to postsecondary institutions to originate loans. Borrowers repay their loans directly to the Federal Government through a private loan-servicing firm contracted by the Department. The Direct Loan program offers a number of repayment plans which borrowers may switch at any time. One option includes the Income Contingent Repayment (ICR) plan, which can extend for up to 25 years, under which borrowers repay based on their income and the amount borrowed. If there is a remaining balance after 25 years, the Government forgives the balance. Under changes brought about by HERA, the Direct Loan standard, graduated, and extended

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FFEL and Direct Loans

repayment plans now conform to the parallel FFEL plans. The CCRAA created a new income-based repayment plan for those borrowers meeting the standard of “partial financial hardship” available to both FFEL and Direct Loan borrowers.

The interest rate on new Stafford and Unsubsidized Stafford Loans starting July 1, 2006 is fixed at 6.8 percent. As in the FFEL program, the CCRAA authorized phased reductions to the interest rates for Subsidized Stafford loans borrowed by undergraduates with the rate cut in half to 3.4 percent on July 1, 2011. The interest rate reverts back to 6.8 percent as of July 1, 2012. The interest rate on new Direct PLUS loans starting July 1, 2006 is fixed at 7.9 percent.

Borrowers under the Direct Loan program pay a 3 percent origination fee on new loans—excluding Consolidation Loans—as of the date of HERA enactment. The 1 percent difference from FFEL is attributable to the 1 percent default fee charged by guaranty agencies to FFEL borrowers. Thus, the combined fee percentages are equivalent between programs. As with FFEL, HERA reduces Direct Loan origination fees by 1 percentage point annually until July 1, 2010, after which origination fees would remain at 1 percent in Direct Loans. The program offers a quarter-point interest rate reduction to Direct Loan student borrowers who repay via electronic funds transfer (i.e., electronic debit).

The CCRAA created a new loan forgiveness program for Direct Loan borrowers who work in public service during a 10-year period while they are repaying Direct Loans. If borrowers still have an outstanding loan balance after 10 years of working in public service and repaying their loans, the Federal Government will forgive the remaining balance on behalf of the borrower. Public service jobs are listed in the law, including public education, public health, government, military service, public safety, public social work, public interest law, or working for a “non-profit” organization as defined by the Internal Revenue Code in section 501(c)(3).

During FY 2007 1,157 schools participated in the Direct Loan program. The Direct Loan program provided \$13 billion in new loans (excluding Consolidations) in FY 2007, accounting for 20 percent of all new FFEL and Direct Loan student loan volume. New Direct Loan volume is expected to grow to almost \$15 billion in FY 2009. (See New Student Loan Volume table, pg. Q-13.) Approximately \$102.4 billion in total Direct Loans were outstanding at the end of FY 2007.

Funding

Both FFEL and Direct Loans are mandatory programs whose costs are largely driven by student loan demand, fueled by increases in the price of postsecondary education and prevailing interest rates. Defaults are also a key component of program costs. The programs are funded by indefinite budget authority and do not require annual congressional appropriations. A loan subsidy—the portion of cost paid by the Federal Government—is calculated for each loan cohort based on the Federal Credit Reform Act of 1990, and reflects the net present value of future cash flows associated with the Direct Loan or loan guarantee.

Administrative costs, paid on an annual cash basis, are not included within the subsidy cost. Subsidy costs for both FFEL and Direct Loans reflect the expected lifetime costs associated with each loan cohort. Budget estimates may show a negative subsidy, indicating that for a given cohort, the estimated present value of program revenues exceeds program costs.

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FFEL and Direct Loans

Both FFEL and Direct Loan programs incur various administrative expenses, some of which are funded through subsidy while most are funded through administrative funds. Prior to the passage of HERA, a mandatory, definite appropriation in Section 458 of the HEA funded the majority of administrative costs in both the FFEL and Direct Loan programs, including account maintenance fee payments to guaranty agencies and administrative costs in Direct Loans, such as loan servicing and student aid information systems. After the HERA, account maintenance fees retained mandatory funding, while the balance of administrative funds became subject to discretionary appropriation as part of the Student Aid Administration (SAA) account. In FY 2009, the Administration requests \$714 million in discretionary funding to administer the Federal student aid programs in the SAA account. This request is discussed in detail in the justification for **Student Aid Administration**, beginning on page Z-1.

Credit Reform Estimates

Student loan program costs are estimated consistent with the Federal Credit Reform Act of 1990. Under the Act, future costs and revenues associated with a loan are estimated for the life of the loan and discounted back to the date of disbursement using Treasury interest rates. Costs related to pre-1992 loans in the FFEL Liquidating account and most Federal administrative costs are statutorily excluded from credit reform calculations. For FFEL, credit reform costs include reimbursements to lenders for in-school interest benefits, special allowance payments to lenders, and default reinsurance payments. These costs are partially offset by student and lender origination fees, negative special allowance payments—referred to as rebates—and collections on defaulted loans.

In the Direct Loan program, cash transactions consist of Government loan disbursements to students, payments of student loan fees, and borrower loan repayments. Defaults and loan discharges reduce future student loan repayments. In FY 2007 through FY 2009, the Direct Loan program reflects a net total positive subsidy (or cost to the Federal Government) due in part to reduced borrower origination fees and interest payments as well as estimated increased costs from a new income-based repayment option and public service loan forgiveness program.

Federal loan programs are often compared using subsidy rates, which represent the Federal cost (the appropriation) as a percentage of loan originations. For FFEL loans originated in 2007, the Budget estimates the weighted average subsidy rate is 6.29 percent: that is, it costs the Government approximately 6.3 cents in appropriations for every dollar of loans it guarantees. For Direct Loans originated in 2007, the weighted average subsidy rate is estimated to be 1.37 percent; that is, the program is projected to spend about 1.4 cents on every dollar originated. Per credit reform rules, other Direct Loan administrative costs are treated on a cash basis.

In an effort to better reflect interest rate variability of future estimates, the Administration in 2006 implemented probabilistic scoring for the FFEL and Direct Loan programs similar to the Congressional Budget Office methodology. Previously, estimates for both the FFEL and Direct Loan programs were developed using point estimates of future interest rates. The updated method factors in the probability that a range of interest rate scenarios may differ from current economic projections.

Under credit reform, the Department annually reestimates the cost of all outstanding loans by cohort to reflect updated modeling assumptions, President's Budget economic assumptions,

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and actual experience. The total change in costs for all outstanding FFEL program account loans at the end of 2007 is reflected as the 2008 reestimate. The 2008 reestimate reflects a net upward component of +\$3.446 billion and a net downward component of -\$2.456 billion for a total net upward reestimate of approximately +\$990 million. That is, the estimated future Federal cost of the approximately \$375 billion outstanding at the end of 2007 is \$990 million higher than was estimated in last year's President's Budget. In FY 2008, the FFEL program also will recognize a modification to those prior loans that were affected by passage of the CCRAA. The downward modification in FY 2008 of almost -\$2.5 billion reflects elimination of lender exceptional performance, reduced guaranty agency retention fees and account maintenance fees.

For the approximately \$102 billion in Direct Loans outstanding at the end of 2007, the Budget assumes net future Federal cost will be higher than estimated in last year's President's Budget. The total change in costs for all outstanding Direct Loan program account loans at the end of FY 2007 is depicted as the 2008 reestimate. The 2008 reestimate reflects a net upward component of about +\$1.158 billion and a net downward component of -\$573.9 million for a total net upward reestimate of over +\$584 million. The upward reestimate requires a current-year mandatory appropriation. Some new provisions in the CCRAA related to income-based repayment options and public sector loan forgiveness resulted in an estimated upward modification to the Direct Loan program of +\$4.1 billion in FY 2008. The Administration is proposing changes to these provisions which, if enacted, would result in savings for future years.

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FFEL and Direct Loans

Loan Terms

The guaranteed FFEL and Direct Loan programs share virtually identical terms and conditions. Both FFEL and Direct Loans provide the following types of loans:

- Stafford Loans are subsidized, low-interest, variable or fixed rate loans based on financial need. The Federal Government pays the interest while the student is in school and during grace and deferment periods. For loans made on or after July 1, 2006, interest rates are fixed at 6.8 percent. The CCRAA authorized a phased reduction to the interest rate for undergraduates borrowing Stafford Loans so that by July 1, 2011 the rate would be cut in half to 3.4 percent for a period of one year. The scheduled reduction follows: 6.0 percent starting July 1, 2008; 5.6 percent starting July 1, 2009; 4.5 percent starting July 1, 2010; 3.4 percent starting July 1, 2011. The rate reverts to 6.8 percent on July 1, 2012.
- Unsubsidized Stafford Loans are low-interest, variable or fixed rate loans that are available to student borrowers, regardless of financial need. The Federal Government does not pay interest accruing on Unsubsidized Stafford Loans. Borrowers may defer payment of interest while in school and have it capitalized until entering repayment. For loans made on or after July 1, 2006 the interest rate is fixed at 6.8 percent.
- PLUS Loans are available to parents of dependent undergraduate students. HERA extends eligibility for these loans to graduate and professional students. The Federal Government does not pay interest accruing on PLUS Loans. For loans made on or after July 1, 2006, HERA provides that the FFEL PLUS interest rate is fixed at 8.5 percent, whereas the Direct Loan PLUS interest rate was unchanged at a fixed rate of 7.9 percent.
- Consolidation Loans allow borrowers with existing student loans to combine their obligations and possibly extend their repayment schedules based on their total student loan debt outstanding. The rate for both FFEL and Direct Consolidation Loans is based on the weighted average of loans consolidated rounded up to the nearest 1/8 of 1 percent.

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FFEL and Direct Loans

DIRECT LOAN AND FFEL PROGRAM LOAN MAXIMUMS		
	ANNUAL LIMITS	
DEPENDENT UNDERGRADUATES	Stafford	Total (Stafford & Unsubsidized Stafford)
First-Year Student	\$3,500	\$3,500
Second-Year Student	\$4,500	\$4,500
Third-Year+ Student	\$5,500	\$5,500
INDEPENDENT UNDERGRADUATES ^{1,2}		
First-Year Student	\$3,500	\$7,500
Second-Year Student	\$4,500	\$8,500
Third-Year+ Student	\$5,500	\$10,500
GRADUATE STUDENTS ²	\$8,500	\$20,500
	AGGREGATE LIMITS	
DEPENDENT UNDERGRADUATES	\$23,000	\$23,000
INDEPENDENT UNDERGRADUATES ^{1,2}	\$23,000	\$46,000
GRADUATE STUDENTS ²	\$65,500	\$138,500

¹ And dependent undergraduates whose parents are unable to borrow under the PLUS program.

² Certain health professions students (independent undergraduates, dependent undergraduates whose parents are unable to borrow under the PLUS program, and graduate students) are eligible to receive increased annual and aggregate Unsubsidized Stafford loan limits due to the phase-out of the HEAL Program. The aggregate Unsubsidized loan limit is \$189,125, less the aggregate amount of any subsidized loans made to the student. **Note:** Students who qualify for only a portion of the maximum Stafford Loan limit may borrow up to the remaining loan amount available under the Unsubsidized Stafford Loan program, limited to cost of attendance minus other aid. For example, a dependent first-year student who qualifies for a \$2,000 Stafford Loan would be eligible for an additional \$1,500 in Unsubsidized Stafford up to the total of \$3,500. For students borrowing under both programs, the Stafford and Unsubsidized Stafford Loan limits displayed above apply.

For independent undergraduate students (or dependent undergraduate students whose parents cannot borrow under the PLUS program) and for graduate and professional students, the maximum a student can borrow during any academic year is: the combined Stafford and Unsubsidized Stafford loan limit shown under the column entitled, "Total (Stafford and Unsubsidized Stafford)." For example, a second-year independent student could borrow up to \$4,500 under Stafford Loans and up to an additional \$4,000 in Unsubsidized Stafford Loans for a total of \$8,500. Under HERA, qualified graduate students are now eligible to borrow PLUS loans, where no limit applies other than cost of attendance. The aggregate loan limit for graduate students is determined by the Secretary of Education.

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FFEL and Direct Loans

Interest Rates Affecting Students, Parents and Lenders

As of July 1, 2006, the student borrower interest rate for new Stafford and Unsubsidized Stafford loans is a fixed rate of 6.8 percent. Stafford loans for undergraduates are subject to interest rate reductions per CCRAA—as noted under Loan Terms, page Q-8. Under current law, for new Stafford Subsidized and Unsubsidized loans that were made on or after October 1, 1998 and before July 1, 2006, the interest rate is based on the 91-day Treasury-bill (T-bill) rate plus 2.3 percent while the loan is in repayment, or plus 1.7 percent during in-school, grace or deferment status. These variable-rate loans are adjusted annually. The July 1, 2007 through June 30, 2008 student borrower interest rate is 6.62 percent during in-school periods and 7.22 percent when the loan enters repayment.

For new PLUS loans disbursed on or after July 1, 2006, the FFEL PLUS interest rate changes to a fixed rate of 8.5 percent, per provisions of HERA, which is an increase over the 7.9 percent provided under P.L. 107-139. Due to technicalities within HERA, the PLUS rate in Direct Loans did not change to 8.5 percent, but is fixed at 7.9 percent. Nevertheless, it appears that congressional intent was to make the PLUS loan interest rate the same under FFEL and Direct Loans. HERA extended PLUS loan eligibility to graduate and professional students. The Higher Education Act (HEA) Amendments of 1998 changed the PLUS interest rate basis from the 52-week T-bill to the 91-day T-bill plus 3.1 percent for PLUS loans made on or after October 1, 1998 and it continues in effect for new loans made before July 1, 2006. For the academic year 2007-08, the PLUS interest rate for loans first disbursed on or after October 1, 1998 and before July 1, 2006 is 8.02 percent.

Effective July 1, 2001, for those PLUS loans that were made on or after July 1, 1994, but prior to October 1, 1998, the rate is based on the weekly average 1-year constant maturity Treasury yield plus 3.1 percent.

Lender Interest Rate

Since January 1, 2000, FFEL lenders earn a guaranteed rate of return, called the special allowance rate based on the average of bond equivalent rates for 3-month commercial paper during a quarter, plus a factor for loans in repayment, and a factor during in-school, grace, or deferment periods. Under current law, FFEL lenders receive the higher of the student interest rate or the special allowance rate. If the student rate is lower than the special allowance rate, the Government makes up the difference. Under HERA, for new loans made on or after April 1, 2006, when the student rate is higher than the special allowance rate, lenders are required to rebate the difference to the Government.

Under CCRAA, the lender special allowance formula factors cited above for most lenders were reduced by 55 basis points to 1.79 percent for loans in repayment and 1.19 percent for loans in an in-school, grace, or deferment period. Eligible non-profit lenders had their special allowance formula reduced by 40 basis points to 1.94 percent for loans in repayment and 1.34 percent for loans in an in-school, grace, or deferment period.

Prior to the passage of the HERA, a PLUS Loan qualified for lender special allowance only if the 91-day T-bill rate plus 3.1 percentage points (set annually for the PLUS interest rate) exceeds 9.0 percent. The special allowance formula uses 2.64 percent added to the commercial paper index for both PLUS and Consolidation Loans. Under HERA, this limitation on PLUS special allowance was eliminated.

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FFEL and Direct Loans

Special Allowance Related to Tax-Exempt Financing

Loans funded with the proceeds of tax-exempt securities originally issued before October 1, 1993, receive substantially higher special allowance payments than are currently paid on other types of loans. These loans have come to be known as “9.5 percent” loans for their higher special allowance treatment. The Taxpayer-Teacher Protection Act of 2004 temporarily limited the ability of loan holders to retain these higher benefits indefinitely by refinancing the underlying securities. These temporary provisions were in effect through December 30, 2005. The HERA made this change permanent and also eliminated “recycling” loans for most loan holders, thereby conforming these older loans to the special allowance rates paid on most other loans.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

BORROWER INTEREST RATES BY ACADEMIC YEAR AND PROGRAM COMPONENT

Type of Loan	Loans made on or after July 1, 1995	Loans made on or after Oct. 1, 1998 ¹	Loans made on or after July 1, 2006
Stafford and Unsubsidized Stafford	91-day Treasury bill rate +2.5%, during in-school, grace, or deferment periods, but T-bill +3.1% during repayment; capped at 8.25%	91-day Treasury bill rate +1.7%, during in-school, grace, or deferment periods, but T-bill +2.3% during repayment; not to exceed 8.25%	Fixed rate of 6.8%. Stafford loans reduced: 6.0%--2008-2009 5.6%--2009-2010 4.5%--2010-2011 3.4%--2011-2012 Resume 6.8% AY 2012
PLUS	Was 52-week Treasury bill rate +3.1%, not to exceed 9%-- as of July 1, 2001 converts to 1-yr constant maturity +3.1%, not to exceed 9%	91-day Treasury bill rate +3.1%, not to exceed 9%	Fixed rate of 7.9% for Direct PLUS; Increased to 8.5% under HERA for FFEL PLUS
FFEL Consolidation Loans²	Weighted average of the interest rates on the loans consolidated, rounded up to the nearest whole percent	Weighted average of the interest rates on the loans consolidated, rounded up to the nearest one-eighth of one percent, not to exceed 8.25%.	Weighted average of the interest rates on the loans consolidated, rounded up to the nearest one-eighth of one percent, not to exceed 8.25%.
Direct Consolidation Loans-- Stafford and Unsubsidized Stafford	91-day Treasury bill rate +2.5%, during in-school, grace, or deferment periods, but T-bill +3.1% during repayment; capped at 8.25%	91-day T-bill rate +2.3%, not to exceed 8.25% for applications received 10-1-98 through 1-31-99. Weighted avg. basis, as above, thereafter.	Weighted avg. basis, as above.
Direct PLUS Consolidation	Was 52-week Treasury bill rate +3.1%, not to exceed 9%-- as of July 1, 2001 converts to 1-yr constant maturity +3.1%, not to exceed 9%	Same as Direct Consolidation above for Stafford and Unsubsidized Stafford loans	Same as Direct Consolidation above for Stafford and Unsubsidized Stafford loans

¹ The Transportation Equity Act for the 21st Century included amendments to the HEA lowering interest rates for new Stafford, Unsubsidized Stafford, and PLUS loans made on or after July 1, 1998, and before October 1, 1998. These same rates were extended with passage of the HEA of 1998 up to July 1, 2003 and extended up to July 1, 2006 through P.L 107-139. These rates are reflected in the chart above, under "Loans made on or after Oct. 1, 1998."

² The Emergency Student Loan Consolidation Act of 1997, which was included in the Department's FY 1998 appropriations act, temporarily changed a number of laws affecting Consolidation Loans. Under this act, which expired September 30, 1998, the interest rate for FFEL Consolidation Loans made on or after November 13, 1997, was calculated based on the Treasury bill calculation--91 Day T-bill + 3.1%, not the weighted average of the interest rates on the loans consolidated.

STUDENT LOANS OVERVIEW

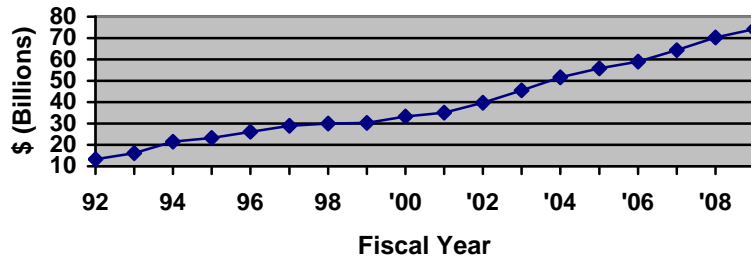
FFEL and Direct Loans

NEW STUDENT LOAN VOLUME

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
New Loan Volume (\$M)							
FFEL	\$33,835	\$39,215	\$43,272	\$46,707	\$51,320	\$56,242	\$59,308
Direct Loans	\$11,742	\$12,449	\$12,570	\$12,176	\$13,022	\$14,103	\$14,867
Total	\$45,577	\$51,664	\$55,843	\$55,883	\$64,342	\$70,345	\$74,174
Number of loans (000s)							
FFEL	8,424	9,555	10,326	10,860	11,519	12,235	12,702
Direct Loans	<u>2,942</u>	<u>3,005</u>	<u>2,971</u>	<u>2,814</u>	<u>2,764</u>	<u>2,857</u>	<u>2,961</u>
Total	11,366	12,559	13,297	13,674	14,283	15,093	15,663

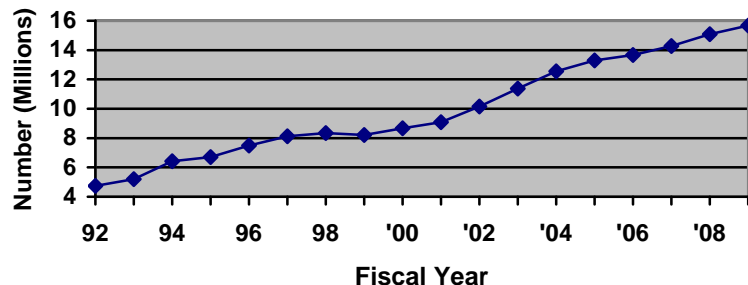
Notes: Details may not sum to totals due to rounding. Loan volume and number of loans reflect net commitments, excluding Consolidation Loans.

**Total New Student Non-Consolidation
Loan Volume**



As shown by these graphs, for FFEL and Direct Loans, both total new loan dollar volume and number of new loans borrowed have increased significantly since 1992 and are projected to continue increasing in 2008 and 2009. A variety of factors such as programmatic changes that increased eligibility, State aid, Federal aid, economic conditions, college costs, and enrollment demographics may interact to affect these demand patterns.

**Total Number of New Loans
(Non-Consolidation)**

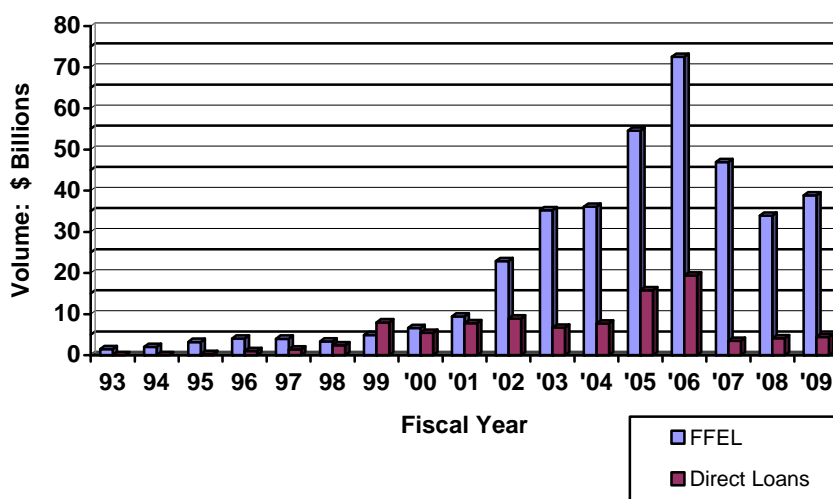


STUDENT LOANS OVERVIEW

FFEL and Direct Loans

Consolidation Loans. A favorable interest rate environment and highly competitive marketing resulted in a dramatic surge in FFEL Consolidation Loan volume from FY 2001 to FY 2006 where volume grew from \$9.4 billion to a record high \$72 billion. Consolidation Loan volume decreased substantially in FY 2007 reflecting a saturated marketplace, an end to “two-step consolidation,” and fixed borrower interest rates. Direct Loan Consolidation Loan volume also increased substantially during this period, growing from \$7.8 billion in FY 2001 to over \$19 billion in FY 2006. While the Direct Loan increase was not as large as FFEL, recent borrowers sought to lock-in lower interest rates in both programs through consolidation, prior to the annual variable in-repayment interest rate jumping from 5.3 percent to 7.14 percent as of July 1, 2006. As in FFEL, Consolidation volume in Direct Loans also decreased substantially in FY 2007, though the Department estimates some increase in demand in 2009.

Consolidation Loan Volume



Subsidy costs—for new loans and reestimates for existing loans—for the past 5 fiscal years are shown below: (\$000s)

	<u>FFEL</u>	<u>Direct Loans</u>
2004	\$5,980,621	\$2,457,222
2005	12,321,033	2,349,124
2006	28,067,662	6,191,320
2007	3,690,487	3,982,176
2008	-397,971	4,983,351

Note: Subsidy costs include net reestimates (combined upward and downward) of prior cohorts and net modifications, which may produce significant annual fluctuations.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

FY 2009 BUDGET REQUEST

The Administration's FY 2009 budget request proposes two student loan policies impacting the FFEL and Direct Loan programs. FFEL new loan subsidies are estimated at \$2.4 billion in FY 2009 and Direct Loan new loan subsidies are estimated at \$328.7 million. The Administration's proposed legislative policies would primarily affect the Direct Loan program, generating over \$1.6 billion in savings in FY 2009 compared to baseline estimates only assuming current law.

Restrict eligibility for the public service loan forgiveness program created in the CCRAA to new loans beginning in the 2009-2010 academic year. (FY 2009-2013 estimated savings: \$1.3 billion). Prior to passage of the CCRAA, the Administration expressed concern that this new program would be costly and inefficient and available only to Direct Loan borrowers. The final language extended this benefit to FFEL loans by allowing consolidation into Direct Loans, potentially disrupting the FFEL program at a time when lenders are already struggling to accommodate the impact of CCRAA provisions. Eliminating retroactivity—so that only new loans are eligible—will allow regulations to be in place before the program becomes effective and allows lenders and servicers to prepare for the new forgiveness program.

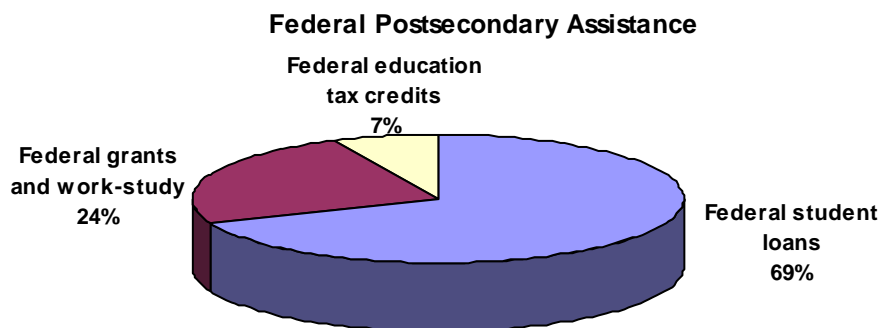
Eliminate the 3-year interest subsidy on Stafford Loans qualifying for income-based repayment (IBR) (FY 2009-2013 estimated savings: \$567 million). Borrowers paying under IBR receive all the same deferment and forbearance benefits as other borrowers. Further, their time spent in these non-repayment periods counts toward the 25 years before their loan is forgiven. (These periods do not count under the regular ICR plan.) In addition, the CCRAA created a new interest subsidy where for 3 years the Government pays the interest portion of the difference between a borrower's IBR payment and what they would pay under a standard 10-year repayment plan. The Department believes the pre-CCRAA deferment benefits, available to all borrowers, are more than sufficient to protect borrowers during difficult financial circumstances.

The Role of Student Loans

A major goal of the Federal student aid program is to assist families in meeting college costs. Federal student loans play a key role in this assistance and constitute the largest component of the Federal postsecondary aid system, accounting for about 69 percent of Federal student aid available in academic year (AY) 2006-2007, based on Table 1a in the "College Board Trends in Student Aid 2007" report (Student Aid Trends). The graph below summarizes the Federal postsecondary aid available in AY 2007.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans



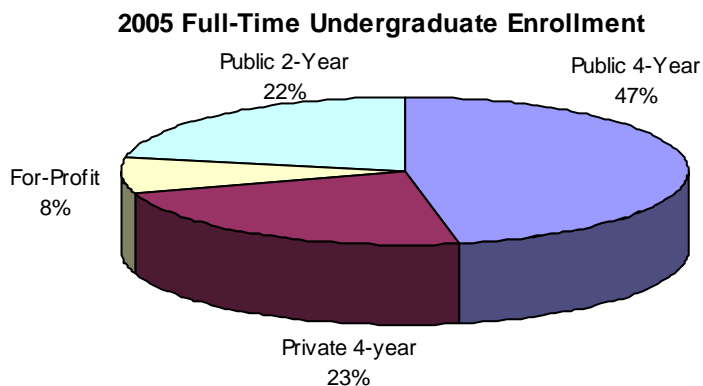
Overall, the Federal Government accounts for about 58 percent of aid used to finance postsecondary education, while State, institutional, and private sources provide 42 percent. The Student Aid Trends report (Table 1b) shows that total Federal aid—including postsecondary education tax credits—increased by 77 percent in constant dollars over a period of 10 academic years (1996-97 to 2006-07). Federal loans have played a significant role over this period, growing by some 61 percent in constant dollars; Pell Grant funding, which is specifically targeted to low-income students, increased by 73 percent.

According to cost of attendance tables (Table 4b) in the 2007 “College Board Trends in College Pricing” (College Pricing) report, the average total cost of attendance (in current dollars) at a 4-year private college increased from \$19,360 in 1997-98 to \$32,307 in 2007-08, representing a 67 percent increase over this 10-year period. Over the same period, the average total cost at a 4-year public college increased almost 82 percent, from \$7,469 to \$13,589. In constant 2007 dollars, after adjusting for inflation, private 4-year college costs increased about 29 percent and public 4-year college costs increased about 41 percent during this 10-year period.

The College Pricing report also cites enrollment data (Table 12a) showing that of all 10.8 million full-time undergraduates in 2005, 47 percent attended public 4-year institutions, 23 percent attended private 4-year institutions, 22 percent attended public 2-year institutions and 8 percent attended for-profit (proprietary) schools. Thus, in the United States about 69 percent of all full-time undergraduates were enrolled in 2- or 4-year public institutions. Overall, full-time undergraduates account for about 62 percent of those enrolled while part-time undergraduates account for about 38 percent. Most of the 6.7 million part-time students—57 percent—attend public 2-year schools. These data help place into context both the cost and attendance patterns at postsecondary institutions.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans



Student Borrowing

The Student Aid Trends report provides data (Figure 4b) on student borrowing using the most recent 2004 National Postsecondary Student Aid Study (NPSAS). Updated data from the next 2008 NPSAS cycle is due to be available in FY 2009. The 2004 study reveals that in the 2003-2004 academic year, about 47 percent of full-time dependent undergraduates at public 4-year schools reported borrowing loans at an average of \$5,390 per borrower (Federal and non-Federal loans), while about 63 percent of full-time dependent undergraduates at private 4-year schools reported borrowing an average of \$7,320. About 17 percent of full-time dependent undergraduates at public 2-year schools reported borrowing an average of \$3,180 and 74 percent of borrowers attending “for profit” schools borrowed loans of \$6,750 on average.

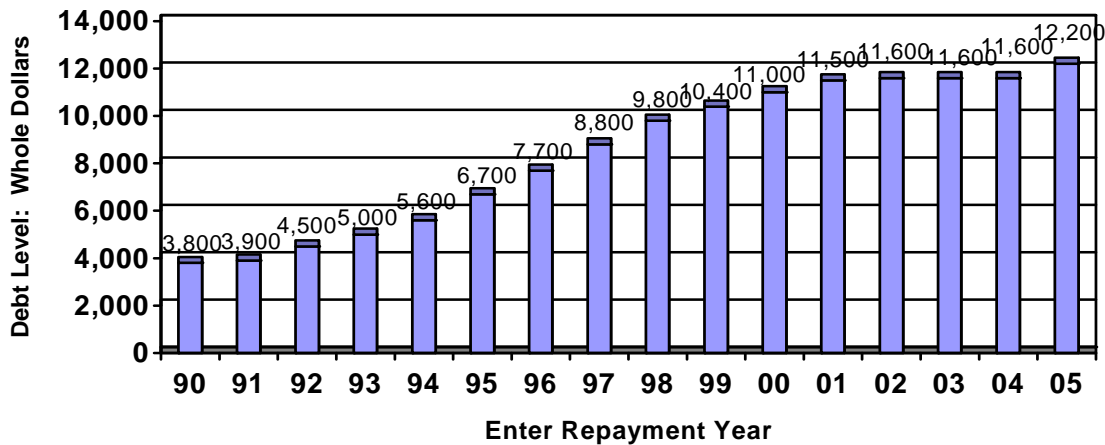
STUDENT LOANS OVERVIEW

FFEL and Direct Loans

Students rely on the Federal loan programs to help close the gap between what their families can afford to pay (“estimated family contribution”) and the cost of attendance (including tuition, fees, and room and board). Based on the latest 2004 NPSAS, about 62 percent of seniors who graduated in 2003-2004 from a 4-year institution reported borrowing a Federal loan at some point in their undergraduate studies. Data available from the 1993, 1996, 2000, and 2004 NPSAS shows the average cumulative Federal debt owed by **undergraduate degree holders** has more than doubled, from \$8,000 reported in 1992-1993 to about \$16,600 in academic year 2003-2004. Nevertheless, the 2004 NPSAS shows little change has occurred to this measure since the 2000 NPSAS.

As shown in the graph below, data from the National Student Loan Data System (NSLDS) reveals that the median level of cumulative Federal borrowing (i.e., Stafford and Unsubsidized Stafford Loans) per student for **all borrowers across all educational levels** has more than tripled since 1990, rising from about \$3,800 to \$12,200 in 2005.

Median Federal Student Loan Debt When Entering Repayment



Program Output Measures on the following pages show program information for FFEL and FDSL program loans for fiscal years 2007 and 2008 consistent with requested funding levels and proposed policies for 2009.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

PROGRAM OUTPUT MEASURES

<u>FFEL Program Loans</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Stafford Loans:			
Loan volume ¹ (million \$)	\$21,713	\$24,050	\$24,866
Number of loans (000s)	6,044	6,458	6,653
Average loan (whole \$)	\$3,593	\$3,724	\$3,738
Subsidy rate ²	17.32%	15.42%	16.67%
Unsubsidized Stafford Loans:			
Loan volume ¹ (million \$)	\$21,400	\$23,384	\$24,696
Number of loans (000s)	4,715	4,988	5,218
Average loan (whole \$)	\$4,538	\$4,688	\$4,733
Subsidy rate ²	-0.19%	-3.73%	-3.07%
PLUS Loans:			
Loan volume ¹ (million \$)	\$8,207	\$8,808	\$9,745
Number of loans (000s)	760	790	831
Average loan (whole \$)	\$10,798	\$11,152	\$11,726
Subsidy rate ²	-1.69%	-5.96%	-5.94%
Consolidation Loans:			
Loan volume ¹ (million \$)	\$46,941	\$33,940	\$38,863
Number of loans (000s)	1,672	1,144	1,264
Average loan (whole \$)	\$28,072	\$29,667	\$30,752
Subsidy rate ²	5.73%	-4.78%	-2.27%
Subsidy Net Reestimates³ (million \$)	-\$3,160	\$990	0
Net Modification⁴ (million \$)	0	-\$2,464	0
Total FFEL Program Loans:			
Loan volume ¹ (million \$)	\$98,261	\$90,182	\$98,170
Number of loans (000s)	13,191	13,379	13,966
Average loan (whole \$)	\$7,449	\$6,740	\$7,029
Net Subsidy cost ³ (million \$)	\$3,690	-\$398	\$2,407
Subsidy rate ²	6.29%	1.07%	2.21%
Outstanding: (billion \$)			
Total FFEL Loans Outstanding	\$375	\$411	\$445
Total Liquidating Loans Outstanding	10	9	9
Total Outstanding ⁵	385	421	454

Details may not sum due to rounding.

¹ Reflects net commitments (disbursements), which are less than amounts committed (e.g., due to loan cancellations).

² This rate generally reflects the Federal cost per new loan dollar. When negative, this rate indicates a net gain to the Government. Reestimates and modifications are not reflected in the subsidy rate.

³ Subsidy amounts are estimated on a net present value basis and include loan net reestimates (of updated interest rates and technical assumptions) and net modifications. A negative subsidy cost results in a net gain to the Federal Government.

⁴ Reflects impact in FY 2008 on prior cohorts from law changes due to CCRAA and in FY 2009 from proposed policies.

⁵ Reflects total FFEL and Liquidating account loan principal (including consolidations) as end of year estimate.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

<u>Direct Loans</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Direct Stafford Loans:			
Loan volume ¹ (million \$)	\$5,781	\$6,248	\$6,453
Number of loans (000s)	1,477	1,526	1,571
Average loan (whole \$)	\$3,914	\$4,093	\$4,109
Subsidy rate ²	10.11%	9.74%	10.80%
Direct Unsubsidized Stafford Loans:			
Loan volume ¹ (million \$)	\$4,918	\$5,307	\$5,597
Number of loans (000s)	1,052	1,086	1,133
Average loan (whole \$)	\$4,673	\$4,887	\$4,939
Subsidy rate ²	-7.84%	-10.31%	-9.97%
Direct PLUS Loans:			
Loan volume ¹ (million \$)	\$2,323	\$2,549	\$2,816
Number of loans (000s)	235	245	257
Average loan (whole \$)	\$9,895	\$10,410	\$10,943
Subsidy rate ²	-8.13%	-11.75%	-11.75%
Direct Consolidation Loans:			
Loan volume ¹ (million \$)	\$3,484	\$4,116	\$4,426
Number of loans (000s)	151	176	187
Average loan (whole \$)	\$23,074	\$23,396	\$23,697
Subsidy rate ²	6.05%	9.88%	9.99%
Subsidy Net Reestimates³ (million \$)	\$3,718	\$585	0
Net Modification⁴ (million \$)	0	\$4,143	-\$1,591
Total Direct Loans:			
Loan volume ¹ (million \$)	\$16,506	\$18,220	\$19,292
Number of loans (000s)	2,915	3,033	3,148
Average loan (whole \$)	\$5,663	\$6,007	\$6,128
Net Subsidy cost ³ (million \$)	\$6,191	\$3,982	\$4,983
Subsidy rate ²	1.37%	0.76%	1.14%
Outstanding: (billion \$)			
Total Direct Loans Outstanding ⁵	\$102	\$107	\$112

Details may not sum due to rounding.

¹ Reflects net commitments (disbursements); which are less than amounts committed (e.g. due to loan cancellations).

² This rate generally reflects the Federal cost per new loan dollar. When negative, this rate indicates a net gain to the Government. Reestimates and modifications are not reflected in the subsidy rate.

³ Subsidy amounts are estimated on a net present value basis and include loan net reestimates (of updated interest rates and technical assumptions) and net modifications. A negative subsidy cost results in a net gain to the Federal Government.

⁴ Reflects impact on prior cohorts from legislative changes due to CCRAA in FY 2008 and proposed policies in FY 2009.

⁵ Reflects total Direct Loan principal (including consolidations) as end of year estimate.

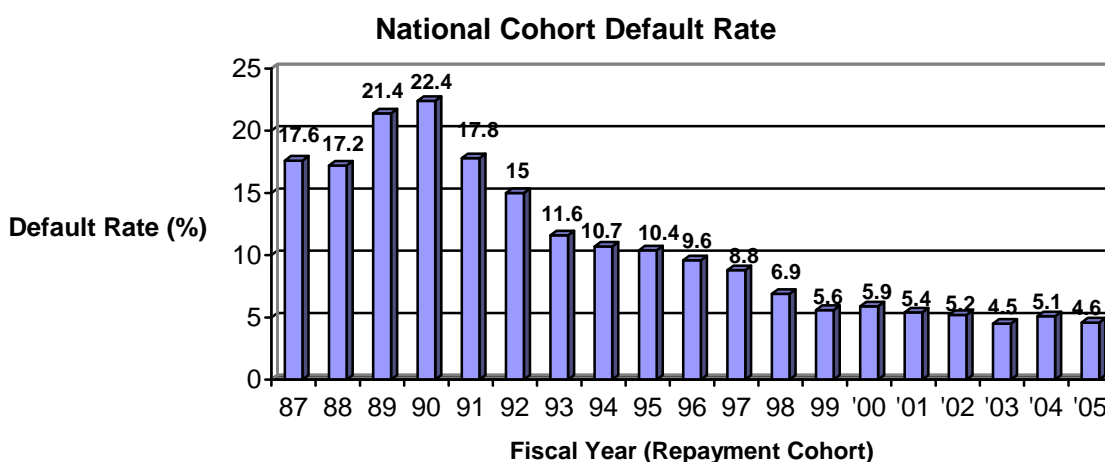
STUDENT LOANS OVERVIEW

FFEL and Direct Loans

PROGRAM OUTCOMES

Loan Defaults. One key measure related to default management is the cohort default rate. The national student loan “cohort default rate” provides a measure of **borrower** default behavior in the first 2 years after entering repayment. This national cohort default rate measure was first established by the Omnibus Budget Reconciliation Act of 1990 (OBRA) to exclude “high-default” institutions from participation in the loan programs. Under current law, these institutions are excluded—for at least 2 years—if they hit or exceed a 25 percent statutory default rate threshold for 3 consecutive years. Since 1993, 1,161 individual schools have lost student loan program eligibility due to high default rates. However, over the past 7 years, the number of institutions facing sanction has dropped markedly. For example, only five schools have been sanctioned over the past 5 years and no schools hit the criteria in the past 2 years.

The national “cohort default rate” (as shown below) measures **borrower** default behavior in just the first 2 years after entering repayment—any defaults occurring outside this statutory period are not incorporated into the default rate for that particular cohort. As a result, this index does not reflect the “lifetime **dollar** default rates” that are used in budget formulation to project future default costs. The lifetime rates account for defaults over the entire life of the loan and are significantly higher than the national cohort rates. Thus, the cohort default rate must be viewed in context with other budget tools.

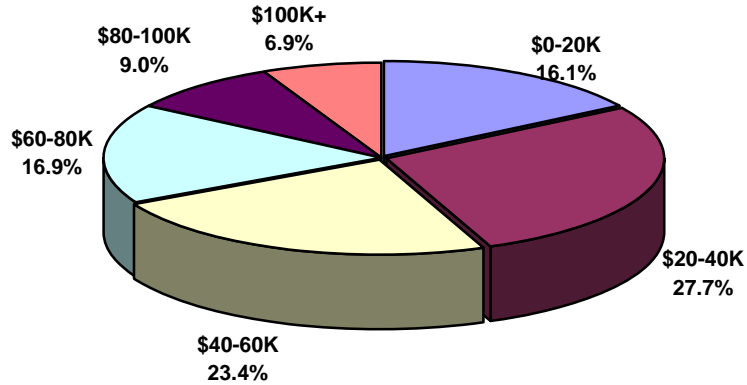


Distribution of Undergraduate Stafford Loan Borrowers by Family Income Category. The Stafford Loan, where the Federal Government pays the interest while the student is in an in-school, grace, or deferment period, is a need-based loan relied on predominantly by low- and middle-income families. Students across many income levels may be eligible for Stafford Loans depending on a number of financial considerations. Unsubsidized Stafford loans complement Stafford, but are not need-based. The following charts reflect the percentage of dependent and independent undergraduate Stafford Loan and Unsubsidized Stafford Loan borrowers at various adjusted gross income family levels according to the most recent NPSAS: 2004 data. Notably, over 67 percent of Stafford dependent borrowers are students from families with under \$60,000 in family income while about 65 percent of the Unsubsidized Stafford dependent borrowers are students from families with over \$60,000 in family income.

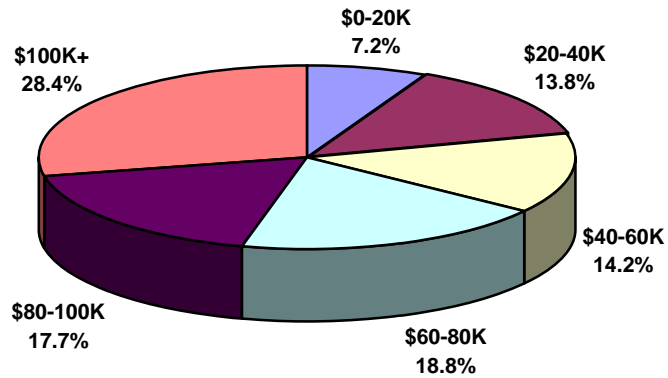
STUDENT LOANS OVERVIEW

FFEL and Direct Loans

Undergraduate Dependent Stafford Loan Borrower Distribution--Source: NPSAS: 2004



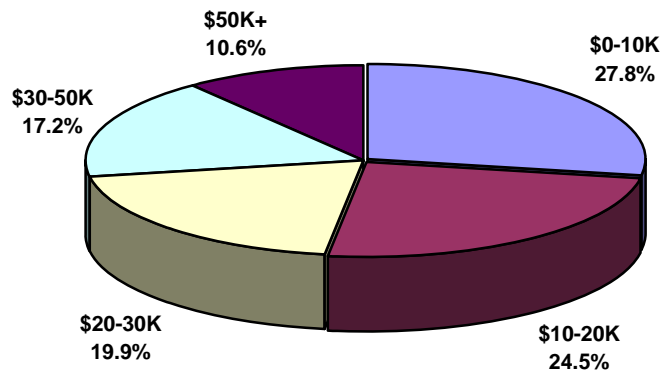
Undergraduate Dependent Unsubsidized Stafford Loan Borrower Distribution--Source: NPSAS: 2004



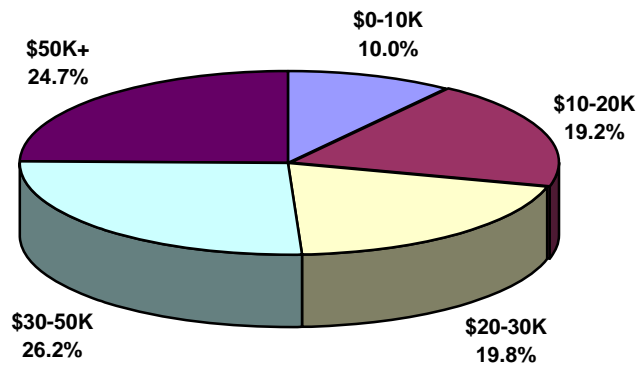
STUDENT LOANS OVERVIEW

FFEL and Direct Loans

**Undergraduate Independent Stafford Loan Borrower
Distribution--Source: NPSAS: 2004**



**Undergraduate Independent Unsubsidized Stafford
Loan Borrower Distribution--Source: NPSAS: 2004**



STUDENT LOANS OVERVIEW

FFEL and Direct Loans

LOAN VOLUME

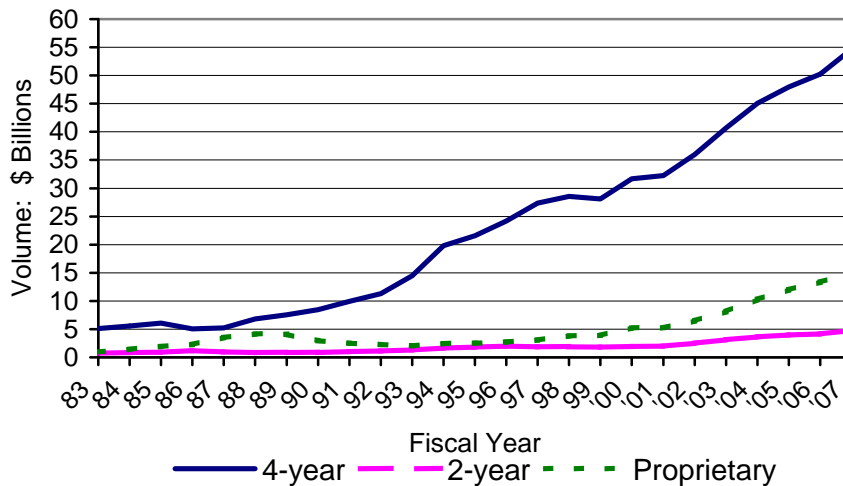
Institutional Sector Trends. Based on FY 2007 NSLDS and related data, 70 percent of all Direct Loan volume occurs at 4-year public institutions, while in the FFEL program 4-year private institutions account for the largest sector of borrowing.

**Distribution of New Loan Volume Dollars by Institution
Within FFEL and Direct Loans**

FY 2007	4-Yr. Public	4-Yr. Private	2-Yr. Public	2-Yr. Private	Proprietary
FFEL	30.8%	39.0%	6.4%	0.5%	23.3%
Direct Loans	70.3%	19.1%	4.1%	0.1%	6.5%

The following graph depicts annual gross commitment loan volume trends by 4-year, 2-year, and proprietary school sectors. (Direct Loan volume data is included beginning with program inception in FY 1994.)

Annual Loan Volume



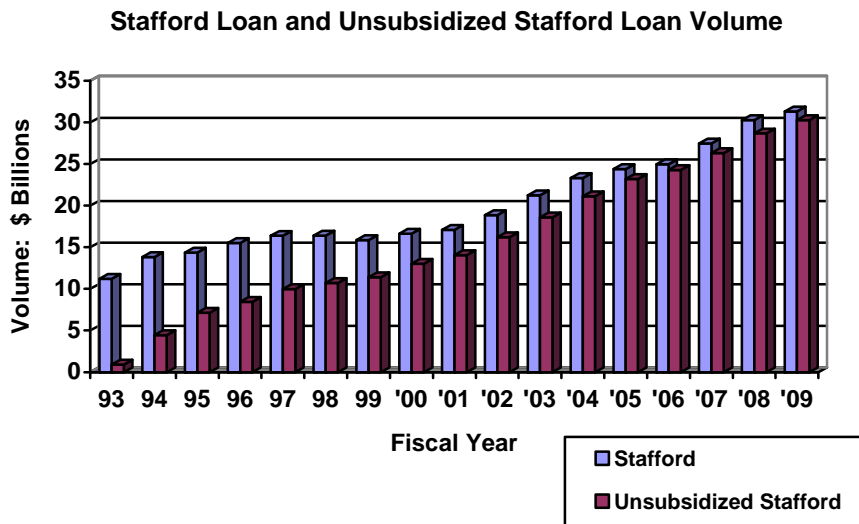
- Loan volume at 4-year institutions continues to show substantial growth, increasing from \$5 billion in FY 1983, to \$54.7 billion in FY 2007, representing 74 percent of all gross commitment loan volume in FY 2007.
- Loan volume at proprietary institutions grew 11.4 percent between 2006 and 2007 and has almost tripled since FY 2000. Nevertheless, at \$14.8 billion in FY 2007, proprietary gross commitment loan volume represents only 20 percent of the total, compared to the 35 percent portion it accounted for in 1988.

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

- Loan volume at 2-year institutions remained steady during the early 1990's, possibly due to relative lower overall cost of attendance. However, volume has increased significantly since then, more than doubling from \$1.9 billion in FY 2000 to nearly \$5 billion in FY 2007. Nevertheless, volume at 2-year schools is comparatively small, accounting for only 6.4 percent of all gross commitment loan volume in FY 2007.

A substantial portion of loan volume growth in the last decade is attributable to the Unsubsidized Stafford Loan program, where students may borrow regardless of financial need. Unsubsidized Stafford Loans have enjoyed strong popularity from inception, as shown in the following graph.



STUDENT LOANS OVERVIEW

FFEL and Direct Loans

PROGRAM PERFORMANCE INFORMATION

Performance Measures

This section presents program performance information, including, for example, GPRA goals, objectives; measures; and performance targets and data; and an assessment of the progress made toward achieving program results. Achievement of program results is based on the cumulative effect of the resources provided in previous years and those requested in FY 2009 and future years, and the resources and efforts invested by those served by this program. The student loan programs and the other Federal student financial aid programs share a common goal of helping remove financial barriers to postsecondary education. Accordingly, these programs share common performance measures, such as student persistence and attainment; these measures are discussed under section N, **Student Financial Assistance**.

Efficiency Measures

The Department has established unit administrative cost as the appropriate efficiency measure for the student loan programs. These programs—and the other student aid programs—have the common goal of helping low- and middle-income Americans pay the increasingly high cost of obtaining a postsecondary education.

Given this shared goal, an analysis of the cost of providing student aid gives Department policymakers and managers a key measure with which to compare the efficient use of Government funding across a variety of delivery mechanisms. In addition, the program-specific unit cost analysis is part of a more comprehensive cost accounting system used by managers at the Department's Federal Student Aid (FSA) office, which has primary responsibility for administering the student aid programs, to monitor operational costs, identify potential processing improvements, and assess the impact of system and organizational refinements.

For the student loan programs, the unit cost reflects the cost of originating loans in the current year and all future costs associated with servicing these loans, forecast out to the year the final loan is retired. Costs in future years are then discounted back to the current year using OMB economic assumptions to determine the overall cost in current dollars of administering that cohort of awards. For example, as can be seen in the table which follows, for the 2002 Direct Loans cohort, discounted future administrative costs total \$453 million with a unit administrative cost of about \$214 per borrower.

Direct Loans and FFEL Unit Costs—2002 through 2004 Cohorts

<u>Programs</u>	<u>2002 Cohort</u>	<u>2003 Cohort</u>	<u>2004 Cohort</u>
Federal Direct Student Loans:			
Origination Costs	\$149,755,883	\$148,159,243	\$107,271,003
Servicing Costs	<u>303,427,034</u>	<u>312,366,241</u>	<u>320,293,462</u>
Total Costs	453,182,917	460,525,484	427,564,465
Number of Borrowers	2,118,598	2,076,802	2,151,824
Unit Costs	\$213.91	\$221.75	\$198.70

STUDENT LOANS OVERVIEW

FFEL and Direct Loans

<u>Programs</u>	<u>2002 Cohort</u>	<u>2003 Cohort</u>	<u>2004 Cohort</u>
Federal Family Education Loans:			
Origination Costs	\$140,056,389	\$147,414,140	\$136,014,159
Servicing Costs	<u>241,022,972</u>	<u>248,123,704</u>	<u>254,420,580</u>
Total Costs	381,079,361	395,537,844	390,434,739
Number of Borrowers	4,875,856	5,991,882	6,611,921
Unit Costs	\$78.16	\$66.01	\$59.05

Total costs for the FFEL 2002 cohort total \$381 million with a unit cost of about \$78 per FFEL borrower. The FFEL program has much of its administrative cost borne by the lenders who actually make the loans; therefore, direct comparisons to Direct Loans may not be entirely significant.

As noted above, these unit costs are based on detailed data from FSA's activity-based cost system, which uses a series of allocation algorithms to generate reports by program, by organizational unit, or by business process for all activities for a given fiscal year. This system, which focuses on expenditures, was applied to annual obligation data to establish baseline costs for each fiscal year. Lifetime costs for each cohort were then calculated based on these baselines. For the loan programs, a methodology for estimating lifetime costs had already been established as part of an exercise for the FY 2006 President's Budget (Budget). A separate methodology was developed for the non-loan programs, where administrative activities occur over a much shorter period.

These unit cost measures for the loan programs differ from unit administrative costs—presented in the President's Budget—in a number of ways. The unit cost measures discussed here reflect administrative costs incurred directly by the Department, regardless of funding source, while the materials in the Budget reflect Federal administrative costs as defined under the Federal Credit Reform Act of 1990. Accordingly, the unit cost measures shown above include costs such as default contract collection costs, which are funded from loan subsidy accounts and therefore excluded from the administrative cost materials in the Budget. Correspondingly, payments to FFEL guaranty agencies from non-subsidy accounts are included in the Budget presentation but excluded from cost measures included in this presentation.

Program Assessment Rating Tool (PART) Issues

Both the FFEL and Direct Loan programs received a rating of "adequate" in 2004, when assessed under the PART criteria established by the Office of Management and Budget (OMB). Generally, FFEL and Direct Loans meet many of the assessment criteria contained in the OMB PART, particularly regarding program purpose, Federal role, and strategic planning. The loan programs have a clear program purpose of helping ensure access to postsecondary education by providing families with needed resources that they would be unlikely to obtain elsewhere. The Federal Government's role here is critical since most private lenders would not be providing loans to students with little or no work experience or credit history.

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In FY 2007, these loan programs provided approximately \$64.3 billion in new loan assistance to almost 8 million qualified borrowers. Both FFEL and Direct Loans are authorized as entitlement programs in order to meet demand.

Based on NPSAS:2004, 46 percent of all undergraduates received Federal financial aid in 2003-04 and about one out of every three undergraduates borrowed a Federal student loan. In 2003-04, of those undergraduates who borrowed a Federal loan, the average amount borrowed was \$5,100. In addition, approximately 40 percent of graduate students borrowed Stafford Loans with the average amount borrowed about \$15,500. Of all professional degree candidates, approximately 74 percent borrowed Stafford Loans, averaging \$22,500 in 2003-04. These statistics provide a key indication of the significant role that the Federal loan programs play in providing access and reducing financial barriers to postsecondary education for a variety of postsecondary students.

Follow-up on PART Findings and Recommendations

The PART improvement plan recommendations for both FFEL and Direct Loan Programs are presented below, followed by a description of the Department's actions to address them.

1) Explore statutory changes in the fiscal year 2007 appropriations process and the reauthorization of the HEA aimed at improving program efficiency, enhancing program stability, and streamlining program operations. The Department is responding by implementing and developing regulations for legislative changes brought about by passage of CCRAA of 2007. New statutory requirements include lower interest rates for undergraduate Subsidized Stafford borrowers, reduced lender special allowance yields, reduced guaranty agency account maintenance fees, a new public service loan forgiveness program, a new income-based repayment option, and developing a competitive loan auction pilot program. Enacting these and other changes will affect borrowers, lenders, and guaranty agencies as well as the Department.

2) Improve the Department's present student loan cost model to more accurately project future cash flows and predict the impact of variables affecting these cash flows. The Department instituted monthly Loan Program Group meetings at which budget, financial, and program staff and OMB examiners monitor program trends, compare actual and estimated costs, and discuss possible and ongoing changes in student loan assumptions and modeling. These meetings supplemented the continuing work of the Credit Reform Work Group (CRWG), through which senior leadership reviewed a broad range of credit reform issues, including student loan cost estimates, credit reform balances and issues related to Department financial statements, and ongoing research such as efforts to develop and expand cohort- and loan-type level balances. The Department is also working closely with OMB to address issues raised in the Presidential Management Agenda's credit reform scorecard.

Both FFEL and Direct Loan programs may be considered for PART review FY 2008.

FY 2009 ESTIMATED PROGRAM SUBSIDY COSTS

The largest loan *subsidy costs* involve in-school interest subsidies for borrowers and costs associated with borrowers who default on their loans. In FY 2009, FFEL costs for new loan subsidies are estimated at \$2.4 billion, supporting approximately \$98.2 billion in total FFEL net commitment volume. Direct Loan new loan subsidy costs in fiscal year 2009 are estimated at \$328.7 million, supporting \$19.3 billion in estimated total Direct Loan net commitment volume.

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Generally, these costs may reflect a combination of positive and negative subsidy by loan type with the relative weightings by loan type and other accounting rules determining the overall positive or negative subsidy cost. A negative subsidy occurs when the present value of cash inflows to the Government is estimated to exceed the present value of cash outflows.

Subsidy rates represent the Federal portion of non-administrative costs--principally interest subsidies and defaults--associated with each borrowed dollar over the life of the loan. Under Federal Credit Reform Act rules, subsidy costs such as default costs and in-school interest benefits are embedded within the program subsidy, whereas Federal administration costs are treated as annual cash amounts and are not included within the subsidy rate. However, based on HERA provisions, the costs of Account Maintenance Fees paid to guaranty agencies which were partially coming out of Direct Loan administrative funds, are, starting in FY 2007, calculated totally as part of the FFEL subsidy cost. This increases FFEL subsidy costs. In addition, the other administrative funds that support Direct Loans which had been categorized as mandatory were, as of FY 2007, no longer mandatory, but subject to annual discretionary appropriations within the **Student Aid Administration** Account.

The subsidy rate for a FFEL or Direct Loan reflects the estimated unit cost per loan to the Federal Government. For example, a \$1,000 loan with Federal subsidy costs of \$100 would have a subsidy rate of 10 percent.

For fiscal year 2009, the weighted average FFEL subsidy rate reflecting proposed policy is estimated at 2.21 percent; while the weighted average Direct Loan subsidy rate reflecting proposed policy is estimated at 1.14 percent. Annual variations in the subsidy rates are largely due to variations in short- and long-term interest rates and technical assumptions. The loan subsidy estimates are particularly sensitive to fluctuations in interest rates. Even small shifts in interest rate projections may produce substantial movement, up or down, in the subsidy rate.

Under HERA, the origination fees paid by students gradually are phased down to zero in FFEL and 1 percent in Direct Loans as of July 1, 2010. Under CCRAA, the reduction to special allowance and account maintenance fees drives FFEL costs down while new loan forgiveness and income-based repayment plans lead to higher Direct Loan costs. Certain policies proposed for FY 2009, such as restricting eligibility for the public sector loan forgiveness to new loans would provide savings in the outlays.

Variations in the subsidy rates between the two loan programs largely exist because borrower repayments in the FFEL program go to lenders, while Direct Loan borrower repayments can be used to offset Federal borrowing and other program costs.

LIQUIDATING ACCOUNT

The cost of FFEL student loan commitments made prior to fiscal year 1992 (the start of credit reform) is appropriated annually under indefinite authority in a Liquidating Account on a cash basis. This account does not issue any new loans, nor estimate loan-lifetime costs by cohort, and does not use a net present value calculation. The Liquidating Account pays pre-1992 student loan activities, such as loan default payments, special allowance payments, and interest benefits. Consequently, as default and in-school interest costs on these older loans decline over time, and recoveries on defaulted loans continue to be collected, annual revenues—also referred to as offsetting collections—will more than offset annual costs, resulting in negative program costs for which no new budget authority is needed. Total net outlays are estimated to

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be -\$553.1 million in FY 2009. This portion of offsetting collections that exceeds program costs is returned to the U.S. Treasury as a capital transfer resulting in net budget savings.

FEDERAL STUDENT LOAN RESERVE FUND

The Higher Education Amendments of 1998 clarified that reserve money held by public and non-profit guaranty agencies participating in the Federal Family Education Loan (FFEL) program are Federal property. These funds are used to pay default claims from FFEL lenders as well as other claims such as those related to death, disability, bankruptcy, and closed schools. The fund, commonly referred to as the Reserve Fund, also pays fees to support successful guaranty agency efforts to avert defaults.

Federal payments reimbursing agencies for default claim payments are paid into these funds, as are borrower insurance premiums based on 1 percent of loan principal. HERA mandates that guaranty agencies are **required** to collect the 1 percent insurance premium—previously optional—on all loans guaranteed or disbursed after July 1, 2006.

The FY 2002 President's Budget clarified that the Reserve Fund should be included on-budget. As required by law, the Reserve Fund returned \$1.085 billion to the Treasury in FY 2002 under a scheduled recall of \$1 billion in reserves mandated by the 1997 Balanced Budget Act, and an additional \$85 million in reserves required to be returned by the Higher Education Amendments of 1998.

The Reserve Fund began FY 2007 with a balance of about \$579 million. The Fund's major revenues are primarily reinsurance payments from the Federal Government and its major expenses are insurance payments to lenders. In addition to these and other cash flows, the Department researched and executed an upward revaluation entry, resulting in an ending balance in FY 2007 of about \$1,105 million that becomes its starting position for FY 2008. As the amount required by HEA, \$82.5 million in guaranty agency reserve funds were returned to the Treasury during FY 2007.