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Student Loan Reauthorization Options [2]

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FEB 18 1997

Note to Barry White and Bob Shireman

From: Aromie Noe AN

CC: Pat Smith, Leslie Mustain, and Tim Rosado

Subject: FYI -- Summary of February meeting of the Advisory Committee of Student Financial Assistance

Date: February 14, 1997

You asked for a summary of the SFA Advisory Committee meeting held last week. Below is a list of highlights.

The meeting opened with McKeon, presenting his view on HEA reauthorization, which was followed by the House and Senate Majority and Minority staff's remarks. Longanecker, McLaughlin, and Hicks presented the President's proposals, ED's work on HEA reauthorization, and updates on Project EASI. In the afternoon, different associations gave their positions on various HEA issues, half of which I missed. There was a 20-minute stint by Senator Wellstone in the afternoon.

Rep. McKeon

- <u>HEA reauthorization principles</u> -- Reiterated the three principles guiding HEA reauthorization included in the House letter sent out to the communities in last December -- making college affordable, simplifying the delivery system, and enhancing academic quality.

- <u>Bipartisan bill</u> -- Emphasized his desire to have a bipartisan bill. He approached Kildee last year and asked him to work together to produce a bipartisan bill.

- <u>Most important goals of HEA</u> -- Stated that the two most important goals of HEA are increasing access to college and assisting middle-income families.

- <u>No preset agenda, but some priority issues</u>

    - Said that he did not have any preset agenda but wanted to work for students.

    - Plans to work on SFA regulations and push for more local control. (He did not elaborate on what he meant by "more local control.")

    - Seemed to think that the current competition between Direct Loan and FFEL is good.

    - After attending a hearing in California, he seemed to be aware of some California issues and asked the Committee members from other States about remedial education. Members from Michigan and Vermont said that remedial education is not an issue for them. (California community college groups want to see no change in the laws allowing the use of Pell Grants for some remedial and ESL education.)

Senator Wellstone

- He made it clear that he did not want to bash the President. He wanted to encourage people to focus on Pell, so he has decided to introduce a proposal to increase the maximum Pell Grant to $5,000. He asked listeners not to concede too quickly to pragmatism on the question of expanding Pell.

Congressional Staffers

Sally Stroup

- House Schedule -- Goodling plans to have a bill ready to go to conference by the end of this year.
- Bipartisan Bill -- Goodling wants to produce a bipartisan bill.
- Tax Proposals and Jurisdiction -- The Republican Committee members and staff do not want the tax committee taking over the education committee as a result of the tax proposals. The Republican members do not want to see people outside the Education Committee making education policy.
- Rep. Goodling's priority issues -- Regulatory relief, maintenance of current SFA funding, and tuition cost control.

Pam Devitt

- Senate Schedule -- The Senate has the same schedule as the House (that is, it aims to produce a bill for conference by the end of this year).
- Structure of each House's bill -- The House and Senate bills would have the same structures, so that conferees/staff can more easily negotiate the differences between two bills. (This is a lesson learned during the attempt to pass a job training bill during the 104th Congress.)
- Concerns over jurisdiction -- Jeffords does not want to discuss reauthorization issues or education policy issues in the context of budget appropriation or reconciliation. He also does not want tax committee members to make education policy.
- Student loan deductibility -- Jeffords supports a tax deduction for student loan interest.
- Jeffords' other views -- He favors more regulatory relief; is very interested in simplifying the system by simplifying FAFSA and slightly tinkering with the current direct loan system (he thinks the competition between two loan programs works well); and will examine the role of technology on campus and any need for changing the current need

analysis formula.

Roger Wolfson (Wellstone's Legislative Assitant)

- Thinks that there is a bipartisan agreement over education being the most important issue, but that there is no such agreement over how to create or deliver the best education system.
- Wellstone's Pell proposal -- Argues that increasing the maximum Pell Grant to $5,000 would help not only low-income but also middle-income families.

Marshall Grigsby (Rep. Clay's Senior Legislative Associate)

- New members and staffers -- There are many new members and staffers who are not at all familiar with HEA, so that a great deal of education is necessary for them.
- Priority issues for Rep. Clay -- Access; debt burden; remedial education (should the Federal government pay for remedial education?); and loan default rates (should the default rate be the determining factor for institutional eligibility?)

David Evans

- Kildee's positions -- Kildee wants to develop a bipartisan bill; views the President's tax proposals favorably; and thinks that increasing a Pell max is encouraging but that we need more than that.
- Jurisdiction issues -- Evans is not very concerned about jurisdiction issues and argues (politely) that people should not be so concerned about these issues. He sounded as if he would be satisfied with creating a dialogue between different Committee members and staffs when they work on postsec education issues.
- Evans' desire to tinker with the HOPE proposal -- Evans seems to want to shift the Administration's grade requirement to using the "satisfactory progress" measure.
- Priority issues -- Having some role for the Federal government in tuition cost control; addressing debt burden issues; focusing on the adequacy of the two loan programs (rather than choosing one program over the other); providing more extensive loan forgiveness programs (especially for those people who pursue a career in teaching, social services, and nursing).

The Department of Education's Presentation

Longanecker and McLaughlin explained the President's proposals. Their explanations were on message. Hicks gave the Department's responses to the Advisory Committee's letter concerning Project EASI. There was only one question about Project EASI.

Higher Education Associations

USSA -- presented a long list of issues with which they are concerned.
- Make Pell an entitlement.

- Preserve SSIG or create a mechanism that ensures the role of State in SFA.
- Provide more funding for SEOG
- Make loan programs more user-friendly; eliminate origination fees; lower interest rates; protect consumer rights.
- Do not increase the current borrowing limits.
- Allow students to put more input in their Work-Study Jobs and help schools to create more meaningful jobs (related to student academic careers or future/professional careers)
- Increase funding for TRIO; make college counseling more accessible.
- Strengthen gatekeeping on vocational/trade schools [e.g., prohibit (or punish) schools that provide false information (graduation rates or job placement records) to students].
- Make Project EASI work.
- Enforce the Campus Security Act more effectively.

Arnold Mitchem

- Increase funding for Talent Search and other early intervention programs; Provide more grant aid (as opposed to loans or tax reliefs).

  [Mitchem argued that TRIO is not an institutional aid but a student financial aid; and that TRIO is not a race-based program but a class-based program.]

Jane Stewart (Kentucky Education Loan Authority)

- Increase funding for need-based programs.
- Regulate schools by sector (collegiate vs. noncollegiate).
- Develop comparable terms and conditions in both Direct Loan program and FFEL.
- Restore the tax deduction for student loan interest payment.
- Reconsider the current default-rate methodology and develop a "structural" default rate as a measurement.

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Bob → ~~**Fax Cover Sheet**~~ → see GA spec's

Number of pages following cover sheet: 10

TO: Pat Smith

FAX: 395-4875

FROM:

Maureen A. McLaughlin ____

Lynn Mahaffie ✓ 708-8928

Tia Cosey ____

Francine Picoult ____

Sandy Wood ____

Janet Sharps ____

MESSAGE:

Pat -

Attached are Dan's GA proposal and revised loan specs.

-Lynn

Draft of 1/16/97

Summary of Proposal to Restructure FFELP Guaranty Agencies

The essence of the Department's proposal to restructure FFELP guaranty agencies is a formal recognition that they do not perform any substantial insurance function but act merely as third-party servicers for a Federal guaranty. The components of the new structure to implement that recognition are as follows:

1. Guarantees. All new guarantees would be issued in the name of the Secretary by guaranty agencies, which would continue to process them on the Secretary's behalf. All existing guarantees would be replaced by direct Federal guarantees, and the guaranty agencies would be relieved of any further contractual liability on them. There would be no risk sharing by the guaranty agencies or adverse economic consequences simply because of high default rates. (See 9, below for noncompliance with regulatory or contractual requirements.) When borrowers default, lenders would have a direct contractual right against the United States for payment within the time frames currently provided for guaranty agencies.

2. Selection/retention. All existing agreements between the Secretary and guaranty agencies would be replaced by agreements conforming to their new role as third-party servicers. These agreements would automatically expire with each reauthorization and might be terminated by the Secretary at any time for substantial failure to meet the performance standards set forth in them (see 9, below) or for specified events of default. Upon expiration, termination or resignation, the Secretary might designate by agreement any State or non-profit agency as the new guaranty agency. At that time, the Secretary might also contract with any other entity, including for-profits, for any or all of the services performed by the former guaranty agency.

3. Reserve funds and assets/capitalization. Guaranty agencies would no longer be capitalized by the Secretary. Existing reserve funds would be recalled to the Department of the Treasury on the following schedule: $731 million in FY98, $127 million in FY99, $186 million in FY00, $186 million in FY01 and $1.271 billion in FY02. During that period, agencies designated by agreement with the Secretary would be allowed to use an aggregate of $350 million of their reserve funds, allocated among them in proportion to their number of outstanding accounts, as interim working capital. The balance of reserves not yet recalled would be invested in specified Government securities, which might be transferred to the Treasury at face value to satisfy any recall requirement. Until recalled, that balance

might not be used for any other purpose and would be placed in escrow, if that is legally feasible. Other reserve fund assets, such as buildings and equipment, might still be used by the guaranty agencies, although they would remain the property of the United States and would be recalled upon cessation of the agency's agreement with the Secretary. Contractors would be required to provide their own working capital.

4. Revenues. The Secretary would pay guaranty agencies designated by agreement $__ for each new guaranty (net of cancellations) and $_ per year for each borrower account. These origination and maintenance fees would be paid quarterly. Other sources of revenue would be a default-avoidance fee paid by lenders (see 6, below), a collections retention (see 8, below), interest on working capital and other FFELP-related business, such as lender escrow and third-party servicing, allowed by the agencies' agreements with the Secretary on an agency-by-agency basis. The current administrative expense allowance and payments for supplemental preclaims assistance would be eliminated. The revenues of contractors would be determined by their contracts.

5. Net revenues. Any net revenues earned by restructured guaranty agencies designated by agreement with the Secretary from activities under those agreements would be the property of the United States but might be used as working capital for those activities. Net revenues in excess of the agencies' working-capital needs might be used to fund need-based grant programs or, if approved by the Secretary, other activities in support of student financial assistance for postsecondary education. Upon cessation of an agency's agreement, all remaining funds would be returned to the Secretary. Any net revenues earned by contractors would be their own.

6. Default prevention. This would be one of the most important functions of restructured guaranty agencies. Lenders would continue to refer delinquent loans to them as they do under current law. If the guaranty agency succeeded in getting a loan current, the lender would pay it a fee of $100 per account. The Secretary would have authority to require refunds of those fees by the guaranty agencies for loans that subsequently default.

7. Claims payment. The Secretary would have authority to pay claims directly to lenders after review by the guaranty agencies. To minimize the need for working capital until a system for direct payments could be put in place, guaranty agencies would be allowed to submit claims immediately after review.

8. Collections. The collections retention would be reduced to 18.5 percent. This rate would make most external collections activities uneconomic and is excessive for internal collections

activities. Accordingly, the Secretary would use existing authority to subrogate defaulted loans to assume all external collections activities as soon as adequate capacity could be established. Under current law, however, the Secretary may reduce guaranty-agency entitlements with the agreement of the guaranty agency. The Secretary would allow guaranty agencies to continue to seek payments internally for periods of time and at retention rates provided by his/her agreements with them. Those rates would be established at levels that did not provide greater incentives for the agencies to seek payment after default than before.

9. Additional performance incentives/disincentives. Guaranty agency agreements would contain specific performance standards, including the submission of timely and accurate data to the Department; and an annual performance audit, based on a statistically valid sample, would be required. Performance results would be measured on a comparable basis and publicly released. Since there would no longer be reinsurance that could be lost for due diligence or other performance failures, guaranty agencies would be required to indemnify the Secretary from any economic loss caused by their performance failures. The Secretary would also have the power to fine guaranty agencies for performance failures. Although indemnification or fines might be paid with Federal working capital, similar to the current situation, any such payment might jeopardize the viability of the agency and would at least reduce the funds available for other authorized uses.

Specs for Student Loan Proposals that are Part of Reconciliation

1. Eliminate the one percent guaranty agency fee and lower the Direct Loan origination fee by one percent for all loans. Reduce origination fees to two percent for subsidized loans in both the FFEL and Direct Loan programs.

Current law: Under the FFEL program, a three percent origination fee and a one percent insurance premium are charged to students at the time a loan is originated. For unsubsidized loans, these fees are authorized by sections 428H(f) and 428H(h) respectively. For subsidized loans, these fees are authorized by section 438(c)(2) and 428(b)(1)(H) respectively. The origination fee for PLUS loans is authorized by 438(c)(6). Currently, some FFEL lenders offer fees lower than the statutory maximum to borrowers.

Under the Direct Loan program, the Department assesses a four percent loan fee (equivalent to the FFEL origination fee plus the insurance premium). This fee is authorized by section 455(c) The Department does not have the authority to waive loan fees or offer loan fees that are lower than the statutory maximum.

Proposed change: Beginning July 1, 1998, eliminate the one percent guaranty agency fee and lower Direct Loan fees by one percent on all loans and reduce origination fees to two percent on subsidized Stafford loans in both programs. [For FFEL loans, delete sections 428H(h) and 428(b)(1)(H) to eliminate the guaranty agency fee, and amend section 438(c)(2) to allow lenders to charge an origination fee of two percent on subsidized loans. For Direct Loans, amend section 455(c) to require the Secretary to charge an origination fee of three percent on unsubsidized loans and two percent on subsidized loans.]

Reasons for changes:

1. One percent reduction for all loans -- The Administration is striving to provide the best possible benefits to students and families. Lowering required fees by one percent for all loans will provide significant benefits to all students and will provide additional funds to students up front when they need funds to pay their tuitions. Lowering fees will also help to standardize benefits between the FFEL and Direct Loan programs, because lenders will no longer be able to reduce costs for FFEL borrowers by waiving the guaranty agency fee.

2. Additional reduction for subsidized loans -- The Administration plans to complement the HOPE scholarship proposal which benefits primarily middle-income students by providing additional student aid benefits to lower-income students. Reducing origination fees an additional one percent for subsidized loans will significantly reduce costs for the neediest students and will provide additional resources to them at the front end of the process.

2. Set in-school interest rate at the ED borrowing rate.

Current law: Beginning in 1998, interest rates on student and PLUS loans will be indexed to the "bond equivalent rate of the security with a comparable maturity." OMB's interpretation of this language is that the interest rate will be indexed to the 10-20 year Treasury rate. In the Direct Loan program, the cost of in-school interest subsidies for Stafford borrowers is the Department's borrowing rate, currently the 10-20 year Treasury rate. (See section 455 (b)(3).) In the FFEL program, the cost of in-school interest subsidies is defined in section 427A(g) and (h). Currently, the rate for loans made on or after July 1, 1995 is the 91-day Treasury bill rate plus 2.5 percent capped at 8.25 percent. For loans made after July 1, 1998, the interest rate is the bond equivalent rate of the securities with a comparable maturity plus 1.0 percent.

Proposed change: Beginning October 1, 1998, the interest rate during in-school, grace, and deferment periods for all Stafford and Unsubsidized Stafford loans will equal the Department's borrowing rate (currently, the 10-20 year Treasury rate). [Amend sections 455(b)(3) and 427A.]

Reason for change: The change will reduce federal costs and provide lower interest rates to borrowers with unsubsidized loans while they are in in-school, grace, and deferment periods. The change also reduces excess profits from the FFEL system by reducing payments to lenders during a time when they have few servicing costs on subsidized loans and the highest profit margins. Finally, the change will standardize interest subsidy payments across the FFEL and Direct Loan programs.

3. Prohibit lenders from providing different terms to different borrowers.

Current law: Currently, some lenders offer better terms such as interest rates and origination fees that are lower than the statutory maximum to some of their least risky borrowers.

Proposed change: Beginning October 1, 1997, require lenders to offer the same terms and conditions to all of their borrowers (*e.g.*, if a lender offers a reduced interest rate or origination fee to some of its borrowers, it must offer those terms to all of its borrowers). Lenders are not prohibited from offering lower interest rates or origination fees to their borrowers as long as they provide these benefits to all of their borrowers.

Reason for change: This change will promote equal costs for all borrowers and ensure that all students served by one lender receive the same benefits regardless of the institution attended or the type of program pursued. This requirement will encourage (but not require) lenders to offer benefits equivalent to those in the Direct Loan program.

4. Provide new repayment plans for FFEL borrowers.

Current law: Currently, many significant differences exist between the Direct Loan and FFEL repayment plans. Direct Loan borrowers may choose between four repayment options, including the standard, income contingent, extended, and graduated repayment plans. In addition, an alternative repayment plan is available to borrowers with unusual circumstances. Borrowers who choose the extended and graduated repayment plans have up to thirty years to repay their loans, depending upon their loan balances. Direct Loan borrowers may change repayment plans at any time with a few regulatory restrictions. (Direct Loan repayment plans are described in section 455(d).)

FFEL borrowers may repay their loans under standard, graduated, or income sensitive repayment plans. However, under all of these plans, borrowers must repay their loans within ten years (excluding periods of deferment and forbearance). Lenders are required to offer graduated and income sensitive repayment plans, but these plans are designed by the individual lenders and vary across the FFEL program. To obtain extended repayment terms, FFEL borrowers must consolidate their loans. (The requirement that FFEL loans be repaid within ten years is in sections 427(a)(2)(B) and 428(b)(1)(D)(ii). Sections 427(a)(2)(H) and 428(b)(1)(E)(i) require FFEL lenders to offer graduated and income sensitive repayment plans. Extended repayment for FFEL consolidation loans is described in section 428C(c)(2).)

Proposed change: By October 1, 1997, require FFEL lenders to offer the same extended, graduated, and alternative repayment plans that are available in Direct Loans in addition to their current standard and income sensitive repayment plans. The parameters of the plans will be outlined in statute, but the specific plans will be determined by the Secretary through regulation. The Secretary will be required by statute to make the standard, extended, and graduated repayment plans the same in the Direct Loan and FFEL programs.

The parameters of the extended and graduated repayment plans will be the same parameters that are currently in the Direct Loan statute (*i.e.*, the extended repayment plan would require a fixed annual repayment amount paid over an extended period of time, except that borrowers must pay at least $600 annually, and the graduated repayment plan would require repayment amounts established at two or more graduated levels and paid over a fixed or extended period of time, except that the borrower's scheduled payments will not be less than 50 percent, or more than 150 percent of the required payment under the standard repayment plan). FFEL lenders will be required to offer income sensitive repayment plans but will design their own plans as they do now.

The statute will also require lenders to provide alternative repayment arrangements to borrowers who demonstrate that the terms and conditions of the other repayment plans do not accommodate the borrowers' exceptional circumstances. The Secretary will provide regulatory guidelines to lenders regarding the definition of exceptional circumstances and the parameters of alternative repayment plans. These guidelines will also apply to Direct Loan servicers.

FFEL borrowers will be permitted to change repayment plans under the same conditions available to Direct Loan borrowers. These conditions will be determined by regulation. However, the statute will require the conditions to be the same in both programs.

Reason for change: This change will provide increased flexibility to FFEL borrowers, allowing them to determine which repayment plans best suit their individual needs. Providing additional repayment plans to FFEL borrowers eliminates the need for consolidation to obtain extended repayment and may avoid some defaults.

The change will also eliminate the differences between repayment terms in the FFEL and Direct Loan programs to the extent possible. (The Direct Loan income contingent repayment plan will not be available to FFEL borrowers, because lenders will not be able to administer the program in a reliable manner that would not excessively burden lenders and borrowers.) Providing similar repayment options among all lenders and programs will simplify the repayment process for borrowers and will allow financial aid administrators to better counsel borrowers regarding repayment of their loans.

5. Provide the same terms and conditions (except income contingent repayment) on all consolidation loans, and eliminate restrictions on consolidation into Direct Loans.

Current law: Currently, the terms of consolidation are more beneficial to borrowers in the Direct Loan program than borrowers in the FFEL program. The statute is very prescriptive regarding the terms of FFEL consolidation loans but provides the Secretary with great discretion regarding the terms and benefits of Direct consolidation loans.

Interest rates -- Section 428C(c)(1) provides that interest rates on FFEL consolidation loans are fixed and are derived from the weighted average of the interest rates of the loans being consolidated. Section 455(g) allows the Department to offer direct consolidation loans with variable interest rates determined in section 455(b).

In-school consolidation -- In FFEL, borrowers may consolidate loans only during grace and repayment periods. (Currently the definition of eligible borrower in 428C(a)(3) does not allow for consolidation when a borrower is in school.) In Direct Loans, borrowers may consolidate during the in-school period, as provided in regulation, as well as during grace and repayment periods.

Consolidation of consolidation loans -- In FFEL, a borrower may not consolidate a consolidation loan and may not add loans to a consolidation loan after a 180-day period. (Currently section 428C(a)(3)(B)(i) terminates eligibility for an FFEL consolidation loan upon receipt of a consolidation loan. Also, section 428(a)(4) does not include consolidation loans in the definition of loans eligible for consolidation.) There are no similar restrictions under the Direct Loan program.

Interest subsidy -- In FFEL, a consolidation loan is subsidized only to the extent that all underlying loans are subsidized. If a borrower consolidates a mixture of subsidized and unsubsidized loans, the entire consolidation loan is unsubsidized. (Section 428C(b)(4)(ii) states that interest will be paid by the Secretary on FFEL consolidation loans that consolidate only subsidized Stafford loans and by the borrower in all other cases.) In Direct Loans, a borrower may consolidate subsidized and unsubsidized loans together without losing the subsidy.

Restrictions on consolidation into the Direct Loan program -- Currently, a borrower cannot consolidate an FFEL loan into a Direct Loan unless the borrower cannot obtain a consolidation loan with an acceptable income sensitive repayment plan. (See section 428C(b)(5).)

Proposed changes:

1. Provide the same variable interest rate to FFEL consolidation borrowers that is available to Direct Loan borrowers. [Amend sections 428C(c)(1) and 428B(e).]

2. Allow FFEL borrowers to consolidate their loans while they are in "in school" status. [Amend the definition of eligible borrower in 428C(a)(3)(A).]

3. Allow the consolidation of FFEL consolidation loans into new FFEL consolidation loans. [Delete the provision in 428C(a)(3)(B) that terminates a borrower's eligibility for a consolidation loan upon receipt of a consolidation loan. However, retain the provision in 428(a)(3)(B)(i)(II) that provides that loans may be added to a consolidation loan during the 180-day period following the making of the consolidation loan. Add FFEL consolidation loans to the list of loans that are eligible for consolidation in section 428C(a)(4).]

4. Eliminate the restrictions on consolidating into Direct Loans. [Amend 428C(b)(5) to allow any FFEL borrower to apply for (but not necessarily receive) a Direct consolidation loan.] [The statute will continue to prohibit consolidation of Direct Loans into FFEL loans, because this would be a sale of a government asset.]

5. Add a provision that would require lenders to retain the interest subsidy on the portion of an FFEL consolidation loan that relates to subsidized loans. [Amend section 428C(b)(4)(ii).]

Reasons for changes: The proposed changes will reduce costs and provide more flexibility to borrowers who obtain FFEL consolidation loans. This change will extend the favorable terms and conditions of Direct consolidation loans to FFEL borrowers, and will streamline the FFEL process for borrowers with multiple lenders who currently do not consolidate because they do not want to lose benefits. These changes will make the benefits of consolidating in FFEL and Direct Loans more similar.

Specifically:

1. Changing the interest rate provides comparable benefits between FFEL and Direct Loan consolidation programs and reduces the cost to FFEL borrowers by providing more market sensitive interest rates. Currently, many borrowers who would like to deal

exclusively with one lender do not consolidate their loans, because it would increase their interest rate. This change would provide a streamlined process for these borrowers.

2. Allowing in-school consolidation in FFEL provides flexibility to FFEL borrowers to manage their personal loan portfolios. Students with loans from multiple lenders may want to consolidate during the in-school period to reduce the amount of paperwork necessary to obtain a deferment.

3. Allowing consolidation of consolidation loans will provide added flexibility to borrowers who return to school, would like to consolidate loans that were formerly ineligible for consolidation, or neglected to include some loans in the original consolidation. This change will allow these borrowers to deal exclusively with one servicer and make only one monthly loan payment as is permitted in the Direct Loan program. This change diminishes the likelihood of delinquency and default on loans excluded from consolidation.

4. Eliminating restrictions on consolidation into Direct Loans provides additional choices regarding consolidation to FFEL borrowers. It will also eliminate the need for borrowers to attempt to consolidate their loans with their current lenders before consolidating into Direct Loans.

5. Allowing FFEL borrowers to retain the interest subsidy when they consolidate provides a financial benefit to borrowers who would like to make one monthly loan payment on all their loans and promotes equal benefits in the Direct Loan and FFEL programs.

6. Compute special allowance rates at the same time and in the same manner as student interest rates.

Current law: Special allowance rates and payments are computed and paid to lenders quarterly under section 438. The basis for special allowance rates is the average Treasury bill auction of the quarter.

Proposed change: Beginning October 1, 1997, compute rates of special allowance annually rather than quarterly based on the last Treasury bill auction of the year. Payments will continue to be made quarterly based on the annual rate. [Amend section 438(b)(2) to provide that the rate of special allowance will be computed annually on June 1st to correspond with the computation of interest rates for students and base the special allowance rate on the preceding year's last auction rather than on the average results during the quarter. Change references throughout the section to "quarterly rate".]

Reason for the change: The purpose of special allowance payments is to assure lenders a fair return on student loans. Special allowance payments guarantee that lenders will earn market rate interest even though student rates are capped. Currently, student interest rates are determined annually and the special allowance rates are computed quarterly. Additionally, interest rates are reset on the basis of the last Treasury bill auction of the year, while special allowances are calculated on the basis of the average auction results during the quarter. These mismatches create the possibility that special allowance will be paid even though the lender is already receiving the prescribed spread. The proposed change will require the calculation of special allowance and student interest rates at the same time and in the same manner thereby eliminating the "partial floor" windfall for lenders.

Bob - FYI this is
what I sent to ED re:
reauthorization. See p.11
recommendation for student
loan ombudsman.
If you have any
questions or ideas, let me
know. I've sent a cc to Pat
Smith as well.
Regards, Betsy

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January 17, 1997

Adam Ochlis
U.S. Department of Education
600 Independence Avenue, S.W.
Room 4050, ROB-3
Washington, D.C. 20202

Dear Mr. Ochlis:

We write on behalf of the Higher Education and Training Access Project (HETAP) of the National Consumer Law Center (NCLC), Public Counsel, and Community Legal Services in response to the call for proposals for reauthorization of the Higher Education Act. NCLC is non-profit organization whose mission is to seek justice for poor Americans struggling with consumer problems. Over the past decade, NCLC has become increasingly involved in student loan problems faced by low-income students, particularly those who have been defrauded by private vocational schools. HETAP is NCLC's consumer advocacy and community education effort on student financial aid and vocational school issues. Public Counsel is the public interest law firm of the Los Angeles County and Beverly Hills Bar Associations. Over the years, Public Counsel has provided assistance to over a thousand victims of proprietary trade school fraud and abuse. Community Legal Services (CLS) is a non-profit agency providing free civil legal representation to the poor in Philadelphia. Over the past seven years, CLS has helped hundreds of low-income students resolve their trade school fraud and student aid problems.

A. <u>Program integrity-- an ongoing concern for students and taxpayers -- must be given precedence over "reducing burdens" on schools.</u>

While anecdotal evidence suggests that the epidemic of problems with scam trade schools experienced in the decade covering 1984-1994 may have subsided, these problems have by no means been eradicated. Staff of the Senate Permanent

Subcommittee on Investigations' noted at a hearing in July 1995 that the problems with proprietary trade schools abound and focused on one egregious example, IADE American Schools based in Los Angeles. Some of the amendments to the HEA in 1992 appear to have made a difference in gatekeeping. In many respects, however, the 1992 amendments did not go far enough, veered off in the wrong direction, or were never fully implemented and therefore failed to achieve the program integrity gains necessary to protect students or the federal fiscal interest. The most glaring example is the State Postsecondary Review Program which was destined to fail because it grouped together of all types of institutions. Great reliance was placed on the SPREs as the means for oversight of high-risk institutions. Without SPREs, other measures must be put in place to preserve program integrity.

As the IADE case illustrates so painfully, enforcement has been lax in all three prongs of the "triad". IADE was monitored, audited, censured, placed on reimbursement, threatened, and reviewed by the state, the accreditor and the Department. Violations were found by all parties that reviewed the school, yet no administrative action was actually ever taken. In part, this is the nature of administrative procedure. Once an entity is accredited, licensed by the state, and certified by the Department as eligible, it is hard to get these imprimaturs of validity removed. Because monitoring and oversight often do not result in sufficient protection of students and public funds and because timely enforcement action often seems nearly impossible, front end gatekeeping is critical. Our discussions with the Department lead us to believe that the Department likewise recognizes the importance of front end gatekeeping.

While no "silver bullet" can assure flawless program integrity, our laundry list of suggestions below sets forth multiple strategies to achieve that goal.

<u>We make the following recommendations for improving front-end gatekeeping and ongoing enforcement for program integrity</u>:

1. ***Create separate standards for vocational schools.*** Reluctance on the part of Congress during the last reauthorization to consider separate standards appears to have subsided in recognition of the fact that differences in mission and operation exist between for-profit and public or non-profit institutions. <u>See, e.g.,</u> 20 USC 1088(a)(3) amendment in 1993 allowing non-profit, degree-granting schools exceptions to the 25% incarcerated students and 50% "ability to benefit" student caps. By scanning the Department's high-default rate and closed school lists on which the overwhelming majority of schools are proprietary trade schools, it is evident that that sector is where the bulk of the Title IV problems lie. Some areas in which to set distinct standards for proprietary schools include:

(a) extending to all proprietary vocational programs the current eligibility requirement for short-term programs of **70% graduation and job placement rates;**

(b) enacting **distinct financial responsibility standards,** such as those in the recent NPRM, for proprietary schools ;
(c) requiring **electronic reporting of financial audits** to the Department in standardized format for easier analysis;
(d) imposing **special consumer disclosure responsibilities** on vocational schools. See section C, infra.; and
(e) statutorily requiring schools that admit ATB students to **maintain proof of high school diploma or its equivalent**, as well as ATB tests and answer sheets, in their files. ATB fraud, including falsification of high school diplomas, has been an ongoing and costly problem. We are at a loss to understand why the Department has apparently reversed its policy requiring maintenance of proof of high school diploma or equivalent, a longstanding, anti-fraud policy. For many years, some states, such as New York, have required trade schools to maintain high school diplomas or the equivalent and have found it quite workable and useful in weeding out fraud.

2. ***Cut off Pell Grant eligibility*** *for schools subject to termination from the loan programs* ***due to high default rates***. We understand that this requirement is temporarily in effect under an appropriations bill, but it should be codified in the HEA.

3. *Vigorously* ***enforce the "85-15 Rule"*** *as written in the HEA*. The new financial responsibility regulation requiring uniform "85-15" reporting on annual audits should make enforcement easier. No statutory change is required or recommended to achieve this recommendation.

4. ***Provisional certification*** *should be the status for all new proprietary institutions, the sector in which the vast majority of Title IV abuses have occurred, for their first five years of participation without renewability of provisional status.* We understand that this is the Department's practice currently. Codifying it would ensure continuity.

5. ***Personal financial guarantees or individual liability*** *should be required* :
a. of school owners of all proprietary **institutions placed on provisional certification**. This recommendation was put forth to the Senate Permanent Subcommittee on Investigations by Assistant Secretary Longanecker in the summer of 1995. It would require deletion of section 498(e)(4) of the HEA;
b. of school owners who knowingly **permit delivery of a grossly deficient educational program** at a proprietary trade school;
c. of school owners and officers **for unmade student loan refunds**. The issue of unmade loan refunds remaining after schools close is a nagging one adversely affecting hundreds of thousands of students and adding greatly to default costs. See section B below for discussion of relief needed for borrowers affected by this abuse.

6. *Impose* ***liability on accrediting agencies*** *that grant or continue accreditation of trade schools that fail to meet prescribed standards.* Accrediting agencies, meant to assure quality of educational institutions and their programs, have failed miserably in the trade school context. For example, scanning the Department's closed school list, the overwhelming majority of schools are proprietaries accredited by the largest trade school accrediting bodies (e.g. nearly 200 locations were accredited by ACCET). Imposing liability on these accreditors when they fail to do their job would give students and the Department an additional party to seek collection from if the school closes. It should also provide theses accreditors with a strong incentive to improve the quality of their work.

7. ***Bar accreditation for institutions until a site visit*** *by the accreditor has been made.* We understand that some accreditors make the site visit and then grant retroactive accreditation, allowing federal dollars to flow before the school has been inspected.

8. ***Hold institutions that appeal high default rates responsible*** *for posting a bond , or require their owners to assume personal liability, to cover the cost of loans to the school during the appeal process , should the appeal be unsuccessful.* While loan default cutoffs have been an effective means for eliminating problem schools from the loan programs, some schools have manipulated default rates and the appeal process in order to delay their ultimate removal from Title IV programs while in the meantime enrolling scores of unsuspecting new students.

9. ***Strengthen "ability to benefit" standards,*** for example by:
(a) excluding ATB borrowers' eligibility for **unsubsidized Stafford loans**, the **statutory limitation** that existed for SLS loans in section 428A of the HEA. When the SLS program was merged into the unsubsidized Stafford loan program, this previous limitation was (probably inadvertently) omitted. We have begun to see trade school students without high school diplomas incurring high-cost unsubsidized Stafford loan debts in addition to subsidized Stafford debts. This sets the students and the Department up for repetition of the SLS default experience. It should be statutorily corrected;
(b) **precluding** Title IV **eligibility for ATB students in correspondence**/distance learning **programs**, because of the particular dangers of ATB falsification posed by these courses of study;
(c) requiring that at least **for-profit schools maintain copies of high school diplomas or GEDs** in order to maintain an audit trail for compliance with ability to benefit provisions. <u>See</u> (A)(1)(e) above;
(d) **maintaining and enforcing the institutional eligibility criteria of 50% ATB students** found in current law, 20 USC 1088(a)(3)(D);
(e) amending the statute to **require that ATB testing be accomplished**

by prospective students taking the GED test, where appropriate, administered by local education agencies. Passing scores for Title IV eligibility purposes could be set by the Secretary on particular sections of the test and could be lower than is required for obtaining a GED. Because administration of the GED tests is secure, it would improve program integrity by removing the testing from the school cite. It could also have the salutary effect of securing GEDs for some students who otherwise might not have sought one; and

(f) as an alternative to the prior recommendation, **setting ATB test passing scores at the mean for high school students** (which is actually lower than for GED recipients). This modest change to the current regulatory standard of one standard deviation below the mean would at least mean that ability to benefit would be slightly closer to high school equivalency than currently. This could be accomplished by regulation.

9. *Amend the HEA, or General Education Provisions Act, to* ***require that schools keep loan-related records for five years after the loan has been paid*** *in full and other Title IV-related records for five years after the last date of attendance.* This should include student attendance records which, in part, provide evidence of "satisfactory progress" for Title IV eligibility purposes.

10. In order to rank schools for program review and enforcement purposes, *create a* ***set of weighted, objective "risk factors"*** *based on the Department's experience with schools that have closed leaving funds owed to students and/or the Department*. We understand that this effort, which would not require statutory changes, is underway at the Department. We urge speedy implementation in order to rationalize targeting of enforcement efforts.

11. ***Increase the use of unannounced visits*** *to suspect schools and* ***start using "shoppers"*** *to pose as prospective students in order to uncover admissions fraud.* Neither of these measures would require new statutory authority. There is no better, and may be no other, way to prove unlawful activity than to surprise the perpetrators. Conversely, advance notice allows unscrupulous schools to alter, hide or destroy key documents. Adelphi Business Schools, for example, became famous for their "moving libraries" which appeared on their campuses only when accreditors or regulators had announced planned visits. To the extent that the Department has reduced its reliance on unannounced visits, we urge reconsideration. Also, shoppers have been used successfully by some state agencies to uncover or confirm complaints, such as those involving falsified ability to benefit testing.

12. ***Maintain the existing caps*** *(no more than 50% of institution's*

courses of study may be correspondence or 50% of its students may be enrolled in correspondence courses) ***for correspondence programs****. Ensure that they also cover "distance learning"; if any new institutional or programmatic eligibility waivers are created for distance learning, limit them t o non-profit schools.* Among the worst abuses of Title IV aid in the 1980's were those committed by proprietary correspondence schools. They recruited unqualified students, grossly inflated the clock hours their lessons represented, routinely created falsified ability to benefit and satisfactory progress records, often had withdrawal rates of 90% and more, and bilked students and taxpayers of millions of dollars. The special difficulties of measuring the quality of correspondence and other distance learning methods militates against allowing for-profit schools to obtain unlimited Title IV funds for such programs.

We are also extremely concerned that the Department's stated goal of easing the regulatory burden on institutions may conflict with protecting students and with the Department's own enforcement capability. As the U.S. Senate Permanent Subcommittee on Investigations was told by the Department's Inspector General in 1995 during hearings on proprietary school abuses of the Pell Grant Program:

> *...it may be inviting to think that, in the context of reinventing government or otherwise, we can do away with prescriptive regulations. However, we must be cautious when applying this approach in an area or to an industry where there is an identified abuse of taxpayer funds and students.... [The] easy availability of huge sums of Federal ... funds provides motivation for some unscrupulous program participants to look for gaps in the existing laws and regulations in order to enhance their own financial interest rather than that of the students or the public. In rendering their decisions, courts will require that regulatory or legislative requirements are clear, and we must ensure that such requirements exist to protect taxpayers and the intended beneficiaries of the [federal] programs.* Statement of John P. Higgins, Acting Inspector General, U.S. Department of Education, to Senate Permanent Subcommittee on Investigations' Hearing on "Abuses in Federal Student Grant Programs and Proprietary School Abuses", July 12, 1995, p. 10 of written statement.

Unless executed with great precision and care, regulatory simplification combined with current federal down-sizing efforts could have a disastrous multiplier effect, crippling enforcement efforts and increasing loan defaults. The Comptroller General has expressed concern that the federal government "has insufficient accounting systems and managers to ensure that ... liabilities [owed to the government] are properly monitored." "U.S. Is Taking On Rising Loan Risk-- As liabilities mount, oversight wanes", article by Jeff Gerth of New York Times, from San

Francisco Chronicle, February 22, 1996, p. A6. De-regulation of the 1980's, numerous reports have shown, allowed booming growth in federal programs, including student loans, without adequate oversight. The result: horrendous student loan default rates, due in large measure to unscrupulous training providers set up exclusively to cash-in on Title IV funding. The tools for preventing unlawful activity by postsecondary institutions must be maintained and strengthened in order to protect students and to prevent the student loan defaults that result from such activity.

Our guiding principle, with which we hope the Department agrees, is that regulatory relief is appropriate only where the regulations do not provide meaningful protection for students or taxpayers. Some recent "simplifications" that have taken place and are still in progress have not necessarily followed that principle. For example:

-Electronic funds transfers (EFTs) of student loan proceeds supposedly make the access to loan funds faster for students, but actually provide faster access for schools and greater control over loan funds by them. Over the past few years, when student advocates have raised growing concern about the loss of student control over loan funds through the use of EFTs, Department and other officials in the student aid industry assured us that the borrower can always maintain control by notifying the school to send back all or part of the loan funds if the student does not enroll, withdraws or simply determines that he or she does not want the total loan amount. The recent Cash Management Regulation (Nov. 29, 1996) attempts to address this problem by allowing a student 14 days from the notice of crediting the student's account with EFT proceeds within which to cancel the loan disbursement. This is a step in the right direction, although we believe the time limit is too short.

-Master checks again simplify the paperwork for lenders and schools, but deprive students of the power of check endorsement. The use of master checks, rather than individual ones also raises questions about tracking individual disbursements.

-Single loan applications for subsidized and unsubsidized Staffords lack an adequate explanation of the differences between the two types of loans. This may cause students unknowingly to incur larger unsubsidized loan debts than they can reasonably repay.

- The period allowed for schools to hold loan proceeds has for many schools become the normal delay in disbursing loan proceeds, i.e. the ceiling has become the floor. This delay allows schools to collect interest on the loan funds, while denying students access to moneys needed for their living expenses. This practice is particularly offensive in the case of unsubsidized loans since the borrower pays interest on the funds while the school holds them.

- Line-of-credit proposals under discussion would also distance borrowers from the process, diminish borrower control over funds, and tend to foster high borrowing. This concept is fraught with dangers for students and for the Department in that uninformed borrowing and over-borrowing will lead to increased loan defaults.

- Record retention rule changes may directly harm the Department's ability to effectively enforce the HEA and regulations. Acceding to institutional complaints about accumulation of paper, the record retention requirements now state that schools must retain loan disbursement documents for only 3 years after the student's last date of attendance. Sometimes Direct Loan schools have a borrower sign a promissory note for the full amount for which he or she is eligible, while disbursing less. The school may record the disbursement electronically and submit it to the servicer, but the disbursement records (e.g. payment to student for funds in excess of tuition, crediting to student's account or other charges) stay at the school. A student may stop attending one school but move on to another, have several years of deferments, and not go into repayment until more than three years after attendance at the first school. Availability of disbursement records is obviously important to borrowers who may have received less in disbursements than the amount on the promissory note, or who may have a claim of forgery or other lack of benefit from the loan proceeds. Disbursement records may also be critical to the Department in proving a collection case. Three years from the last date of attendance is simply not long enough for principal balance disputes to surface and be addressed.

In summary, program integrity is an ongoing concern for students and taxpayers and must not be relegated by the Department to a secondary role. Any regulatory relief urged by postsecondary institutions, lenders, or others should not be undertaken unless a finding is made that it will not adversely affect student protections, the Department's and the Inspector General's enforcement efforts, and the federal fiscal interest.

B. The lingering effects of trade school fraud and need for borrower redress

The Higher Education Act (HEA) has enabled countless low- and moderate-income individuals who otherwise would have been unable to do so to obtain high quality education and postsecondary training. In so doing, the HEA, like the GI Bill before it, has opened the door to the American dream for millions of Americans. Unfortunately, it has also slammed the door shut on hundreds of thousands of low-income Americans by allowing unscrupulous trade schools to flourish and to hoodwink those most desperate for self-improvement into obligating themselves for loans to pay for worthless job training. The tragic result is students left with little or no training, no jobs, substantial debts they cannot possibly repay, ruined credit ratings, and ineligibility for further student aid to get a real education or high quality training.

Certain provisions in the 1992 amendments to the HEA, notably the closed school and false certification discharge provisions, provided relief to some of those victimized by unlawful or unethical trade school activity. We strongly support those provisions and urge no modification to them. What is called for is implementation by the Department and the guaranty agencies to effectuate the beneficent purpose of the discharge provisions. We strongly urge the Department to work with us on a public service information campaign to ensure that all eligible students are reached and receive the loan cancellation to which they are statutorily entitled. Anecdotal evidence suggests that: (1) a large percentage of the defaulted borrowers eligible for closed school discharge have been unreachable due to inaccurate addresses in the hands of loan holders; and (2) only about 20% of the defaulted borrowers identified by guarantors as potentially eligible for closed school discharge and to whom notices of discharge rights have been sent even respond. Clearly, more needs to be done to reach out to these borrowers whose loans may go back as far as 1986 and who, therefore, otherwise may be lost to the system.

Furthermore, as the Department knows, the 1992 provisions reach only a small segment of those who have suffered set backs from their experience with fraudulent trade schools. We believe that the Department already has sufficient statutory authority to cease collection of student loan balances owed by students whose school owes but failed to pay loan refunds on their behalf and then closed. The Department previously had indicated that it would by regulation provide relief to this group of students, but has not yet done so. We strongly urge you to provide relief for these students by using your regulatory authority, or if deemed necessary, by seeking statutory authority.

Recommendations (none of which require statutory amendments):

1. **Maintain, as written, the closed school and false certification discharge provisions** and implement them fully.

2. **Embark on a public education campaign**, including public service announcements, working with students' advocates **to inform borrowers of their discharge rights.**

3. Step up recoupment activity against closed schools, their principals and affiliates.

4. **Discharge loan balances**-- both prospectively for new loans and retroactively for existing balances-- **for students whose schools owed but never paid loan refunds** on their behalf and which have closed.

C. **<u>Improving information available to students in order to reduce bad choices and consequent loan defaults</u>**

The availability of comparative consumer information on training programs may not save all prospective students from poor educational experiences. Unsophisticated and poor people desperate to better their situation may instead succumb to high pressure sales tactics. Nevertheless, without basic, comparative data it is impossible for consumers to make informed choices. Essential information for trade school students includes graduation rates; licensing examination pass rates, if applicable; and placement rates, showing the number of graduates who got the job for which they had trained (and not merely a "related job") within six months of graduation and who kept the job for at least four months. This information was required under prior Departmental regulations. We had urged such expanded information In our comments on the Right-to-Know Act regulations. We, again, strongly recommend that such data-- verified for accuracy-- be provided to prospective students and be compiled for distribution on a comparative basis by the Department.

Many other sources of information on schools should also be made available through the Department to students and their human services counselors and advocates. For example, we strongly urge that the Department continue developing the Postsecondary Education Participants System (PEPS) to encompass data from all Departmental sources, accreditors, and state agencies and make this information accessible to the public, perhaps electronically. The National Student Loan Data System (NSLDS), already up and running and accessible by institutions, should also be available to students in order to help them track their loans and other aid.

Regarding deferments, a confusing array of possibilities exist for borrowers depending on when their loan promissory notes were signed and when the proceeds were disbursed. The only statutory requirement for notification of deferment rights is that they be contained in the promissory note. Borrowers are often unaware of these rights. Thus, some entitled to postponement of the repayment obligation may unwittingly slip into default. More meaningful notice of deferment rights-- after leaving school-- should be given.

<u>Recommendations</u>:

1. Amend the HEA to **require schools that predominantly provide vocational training programs to provide**, in a uniform format, **data** on their graduation, placement (as defined above), and licensure exam pass rates. Vocational training institutions already retain the responsibility to compile the data under many state licensing laws and accrediting body standards. The statute should require that they provide the data to prospective students and to the Department. The Department would compile the data in comparative format for dissemination to the public. By including programs offered by both proprietary and non-proprietary institutions,

prospective students will be able to engage in much more comprehensive comparison shopping. The data should be verified by some outside source, such as attestation by a certified public accountant, and should remain auditable by government entities.

2. **Make development of PEPS**, as a thorough data base, **a priority** to carry out the mandate of section 498A(a)(3) of the HEA and amend the statute to clarify public access to the data.

3. **Ensure that students have access to NSLDS** data on their own student aid. This would enable students and their advocates to locate the holders of their student loans far more easily than can be accomplished currently. This would not require a statutory amendment.

4. Amend the statute to **require lenders or guarantors**, or the Department in the case of the Direct Loan Program, **to notify borrowers of their deferment rights** and to make deferments retroactive to the date of delinquency upon the borrower's showing that he would have been so entitled had he timely applied.

D. Increased funding for Adult Literacy Training

We know that the President is concerned with literacy issues and has proposed the use of volunteer literacy tutors and work study student tutors, a worthwhile endeavor which we support. But in order to make significant headway in the war against illiteracy, funds must be committed to provide the expertise of trained reading instructors both for students and to train lay tutors. The adult population, an increasing percentage of those seeking higher education and job training, is especially hard to reach and yet must not be forsaken.

Recommendation: We suggest that the aim of our national education policy should be raising literacy levels and increasing the percentage of those with high school diplomas and equivalencies rather than allowing to grow the number of ATB students receiving aid meant for those in higher education. We strongly urge the Department to fight for increased funds for localities under the Adult Literacy Act and to embark on a national adult literacy campaign.

E. Massive confusion in the student loan programs warrants an ombudsman program for student loan problems as a means for default avoidance

Some student advocates spend much of their work life trying to help students sort out complicated student loan problems like the following that never should have happened:

*a lump sum loan payment rather than delay the next payment date as intended, mistakenly hurled the borrower into default;

*a deferment granted on 5 of the student's 6 loans held by the same entity erroneously was not granted on the sixth and put the student into default, collection fees, and ineligibility for further aid to finish her last semester;

* a student whose Direct Loan is promptly, electronically received by the college can't get the excess proceeds for weeks because the college is holding them for the maximum allowable period-- although the student needs the loan proceeds for food and is accruing interest charges on the unsubsidized portion of the loan on which is earning interest.

Students trying to pay their loans and avoid default are increasingly tripped up by computer glitches, lost mail , and other administrative problems that are virtually impossible to untangle. As *Smart Money Magazine* put it, such students "get caught up in a maelstrom of bureaucratic bumbling, computer systems gone wild, misplaced paperwork, and even thuggish collection agencies. It's a tale of borrowers-- and there are thousands of them-- who've had their lives disrupted or even been put into default because of a mistake by their loan servicer or guaranty agency." "Getting the Third Degree", by Devin Leonard, March 1996, p. 108.

Few lawyers or other advocates have expertise in student loan issues at all, let alone the detailed and frequently changing regulations and actors. An Ombudsman Program, properly funded and staffed and with enough independence to be a strong advocate for borrowers and not an apologist for any systemic or individual failings, could serve several important functions. It could resolve individual borrowers' loan problems, thereby reducing defaults, and track systemic patterns.

We note that the California Student Aid Commission and Texas Guaranty Agency each have new ombudsman offices. While these may serve a useful role for loans held by those agencies, many borrowers have loans guaranteed or held by multiple agencies, agencies that may not have ombudsman offices, or have loans held by the Department either because they are Direct Loans or are FFEL loans in default and assigned to the Department. We also note that the Department has recently established a toll-free Customer Support Branch Inquiry Service for financial aid professionals. Dear Colleague GEN-96-12. The stated purpose of the new hotline is to provide a means to "cut through the red tape", with a 3 day turn around for questions from financial aid administrators. If students are truly viewed as the Department's number one customer, the Department should also provide a meaningful way to cut through student loan red tape in order to help borrowers avoid defaults.

Recommendation: Create an independent Ombudsman Office for resolving student loan complaints. One successful model for an ombudsman program is found in the Older Americans Act, 20 USC 3058g. The Student Loan Ombudsman Office could be part of the Department of Education housed in Washington or in one or more of the regional offices. Or the Ombudsman function could be contracted out to non-profit groups meeting strict eligibility guidelines. One funding mechanism would be to impose on lenders and/or guarantors, the parties seeking to perpetuate the complex

FFEL program, a small fee per loan guaranteed. This funding mechanism obviously would require a legislative amendment.

F. Structuring the HOPE Tax Credit Proposal to Help the Poor

From the perspective of the poor, the HOPE education/tuition tax credit proposal has two flaws. First, unless the credit is refundable and applicable to very low levels of adjusted gross income it will not put any dollars in the pockets of people earning less than 150% to 200% of the poverty level. Secondly, getting a $1500 tax credit in April will not enable those with no discretionary income to pay community college tuition for the previous September or January.

The refundability issue is critical to the millions of individuals who have relied, in part or solely, on welfare for income support prior to the 1996 changes in federal law. While many of those individuals have some amount of earned income each year, typically it would be an amount well below the minimum income to incur a positive tax liability, especially after taking into account the Earned Income Tax Credit (EITC). It would indeed be ironic if the EITC, part of the Administration's effort to "make work pay", prevented low-income workers from receiving money for their education through the new education tax credit. Like the EITC, the education tax credit formula should, therefore, allow workers with any amount of earned income to receive some refundable credit, and should be phased out at higher levels of income.

The delayed reimbursement issue is not readily solved. Certainly, the education tax credit should be eligible for the same advance payment system that is now allowed for the EITC (by having employer withholding reduced). That way, at least some low-income beneficiaries of the HOPE credit would get help with living expenses, while perhaps relying on Pell grants or other sources to pay for tuition and books.

We strongly urge the Department to focus its efforts on a refundable tax credit that would kick in at low income levels in order to realize the President's goal of putting community college within the reach of every American, as opposed to unlimited tax deductions that would primarily benefit high-bracket, affluent taxpayers.

Thank you for this opportunity to comment. We look forward to continuing to work with the Department and the Congress to improve students' access to high quality education and training programs under the Higher Education Act .

Very truly yours,

Elizabeth M. Imholz

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January 30, 1997

Hon. William F. Goodling, Chairman
Committee on Education and the Workforce
United States House of Representatives
Ford House Office Building (Room 230)
Washington, D.C. 20515

Dear Chairman Goodling:

Set forth below are the joint recommendations of several non-profit groups representing the interests of students for reauthorization of the Higher Education Act. These groups include the Higher Education and Training Access Project (HETAP) of the National Consumer Law Center (NCLC), the U.S. Student Association (USSA), Public Counsel, and Community Legal Services. In addition to representing individual students, representatives of each group have participated in negotiated rulemaking with the Department of Education from 1992-1995. The undersigned representative of HETAP also participated in the 1992 reauthorization and has testified before both Senate and House committees in that connection. These recommendations do not present statutory language, which we intend to provide at a later point.

NCLC is non-profit organization whose mission is to seek justice for poor Americans struggling with consumer problems. Over the past decade, NCLC has become increasingly involved in student loan problems faced by low-income students, particularly those who have been defrauded by private vocational schools. HETAP is NCLC's consumer advocacy and community education effort on student financial aid and vocational school issues. USSA, founded in 1947, is the nation's oldest and largest student organization. USSA currently represents more than 3 million students at over 300 campuses nationwide. Public Counsel is the public interest law firm of the Los Angeles County and Beverly Hills Bar Associations. Over the years, Public Counsel has provided assistance to over a thousand victims of proprietary trade school fraud and abuse. Community Legal Services (CLS) is a non-profit agency providing free civil legal representation to the poor in Philadelphia. Over the past seven years, CLS has helped hundreds of low-income students resolve their trade school fraud and student aid problems.

A. <u>Program integrity-- an ongoing concern for students and taxpayers -- must be given precedence over "reducing burdens" on schools.</u>

While anecdotal evidence suggests that the epidemic of problems with scam trade schools experienced in the decade covering 1984-1994 may have subsided, these problems have by no means been eradicated. Staff of the Senate Permanent Subcommittee on Investigations' noted at a hearing in July 1995 that the problems with proprietary trade schools abound and focused on one egregious example, IADE American Schools based in Los Angeles. Some of the amendments to the Higher Education Act (HEA) in 1992 appear to have made a difference in gatekeeping. In many respects, however, the 1992 amendments did not go far enough, veered off in the wrong direction, or were never fully implemented and therefore failed to achieve the program integrity gains necessary to protect students or the federal fiscal interest. The most glaring example is the State Postsecondary Review Program which was destined to fail because it grouped together all types of institutions. Great reliance was placed on the SPREs as the means for oversight of high-risk institutions. Without SPREs, other measures must be put in place to preserve program integrity.

As the IADE case illustrates so painfully, enforcement has been lax in all three prongs of the "triad". IADE was monitored, audited, censured, placed on reimbursement, threatened, and reviewed by the state, the accreditor and the Department. Violations were found by all parties that reviewed the school, yet no administrative action was actually ever taken. The owner and the financial aid director of IADE recently were indicted for defrauding the federal government of more than $1 million in Pell grant funds. As the IADE example illustrates, once an entity is accredited, licensed by the state, and certified by the Department as eligible, it is hard to get these imprimaturs of validity removed. Because monitoring and oversight often do not result in sufficient protection of students and public funds and because timely enforcement action often seems nearly impossible, front end gatekeeping is critical.

While no "silver bullet" can assure flawless program integrity, our laundry list of recommendations below suggests multiple strategies to achieve that goal.

<u>We make the following recommendations for improving front-end gatekeeping and ongoing enforcement for program integrity</u>:

1. ***Create separate standards for proprietary vocational schools.*** Increasingly, Congress has recognized that separate standards for trade schools are appropriate based upon the difference in mission and operation between for-profit and public or non-profit institutions. <u>See, e.g.,</u> 20 USC

1088(a)(3) amendment in 1993 allowing non-profit, degree-granting schools exceptions to the 25% incarcerated students and 50% "ability to benefit" student caps. Scanning the Department's high-default rate and closed school lists on which the overwhelming majority of schools are proprietary trade schools, it is evident that that sector is where the bulk of the Title IV problems lie. Some areas in which to set distinct standards for proprietary schools include:

(a) extending to all proprietary vocational programs the current eligibility requirement for short-term programs of **70% graduation and job placement rates;**

(b) enacting **distinct financial responsibility standards,** such as those in the recent NPRM published by the Department, for proprietary schools ;

(c) requiring **electronic reporting of financial audits** to the Department in standardized format for easier analysis;

(d) imposing **special consumer disclosure responsibilities** on vocational schools. See section C, infra.; and

(e) statutorily requiring schools that admit students without high school diplomas or GEDs ("ability to benefit" or ATB students) to **maintain proof of high school diploma or its equivalent**, as well as ATB tests and answer sheets, in their files. ATB fraud, including falsification of high school diplomas, has been an ongoing and costly problem. We are at a loss to understand why the Department has apparently reversed its policy requiring maintenance of proof of high school diploma or equivalent, a longstanding, anti-fraud policy. For many years, some states, such as New York, have required trade schools to maintain high school diplomas or the equivalent and have found it quite workable and useful in weeding out fraud.

2. ***Cut off Pell Grant eligibility*** *for schools subject to termination from the loan programs* ***due to high default rates***. We understand that this requirement is temporarily in effect under an appropriations bill, but it should be codified in the HEA.

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4. ***Provisional certification*** *should be the status for at least all new proprietary institutions, the sector in which the vast majority of Title IV abuses have occurred, for their first five years of participation without renewability of provisional status.* We understand that this is the Department's practice currently. Codifying it would ensure continuity.

5. ***Personal financial guarantees or individual liability*** *should be required* :
(a) of school owners of all proprietary **institutions placed on provisional certification**. This recommendation was put forth to th Senate Permanent Subcommittee on Investigations by Assistant Sec 'ary Longanecker in the summer of 1995. It would require deletion of sec' 498(e)(4) of the HEA;
(b) of school owners who knowingly **permit delivery of a grossl deficient educational program** at a proprietary trade school;
(c) of school owners and officers **for unmade student loan ref ds**. The issue of unmade loan refunds remaining after schools close a nagging one adversely affecting hundreds of thousands of students and adding greatly to default costs. See section B below for discussion of relief needed for borrowers affected by this abuse.

6. *Impose* ***liability on accrediting agencies*** *that grant or continue accreditation of trade schools that fail to meet prescribed standards.* Accrediting agencies, meant to assure quality of educational institutions and their programs, have failed miserably in the trade school context. For example, reviewing the Department's closed school list, the overwhelming majority of schools are proprietaries accredited by the largest trade school accrediting bodies (e.g. nearly 200 locations were accredited by ACCET). Imposing liability on these accreditors when they fail to do their job would protect the federal fiscal interest by giving students and the Department an additional party to seek collection from if the school closes. It should also provide theses accreditors with a strong incentive to improve the quality of their work.

7. ***Bar accreditation for institutions until a site visit*** *by the accreditor has been made.* We understand that some accreditors make the site visit and then grant retroactive accreditation, allowing federal dollars to flow before the school has been inspected.

8. ***Hold institutions that appeal high default rates responsible*** *for posting a bond , or require their owners to assume personal liability, to cover the cost of loans to the school during the appeal process , should the appeal be unsuccessful.* While loan default cutoffs have been an effective means for eliminating problem schools from the loan programs, some schools have manipulated default rates and the appeal process in order to delay their ultimate removal from Title IV programs while in the meantime enrolling scores of unsuspecting new students.

9. ***Strengthen "ability to benefit" standards,*** for example by:
(a) excluding ATB borrowers' eligibility for **unsubsidized Stafford loans**, the **statutory limitation** that existed for SLS loans in section 428A of the

HEA. When the SLS program was merged into the unsubsidized Stafford loan program, this previous limitation was (we assume inadvertently) omitted. We have begun to see trade school students without high school diplomas incurring high-cost unsubsidized Stafford loan debts in addition to subsidized Stafford debts. This sets the students and the Department up for repetition of the SLS default experience. It should be statutorily corrected;
(b) **precluding** Title IV **eligibility for ATB students in correspondence/**distance learning **programs**, because of the particular dangers of ATB falsification posed by these courses of study;
(c) requiring that at least **for-profit schools maintain copies of high school diplomas or GEDs** in order to maintain an audit trail for compliance with ability to benefit provisions. See (1)(e) above;
(d) **maintaining and enforcing the institutional eligibility criteria of 50% ATB students** found in current law, 20 USC 1088(a)(3)(D); and
(e) amending the statute to **require that ATB testing be accomplished by prospective students taking the GED test**, where appropriate, administered by local education agencies. Passing scores for Title IV eligibility purposes could be set by the Secretary on particular sections of the test and could be lower than is required for obtaining a GED. Because administration of the GED tests is secure, it would improve program integrity by removing the testing from the school cite. It could also have the salutary effect of securing GEDs for some students who otherwise might not have sought one.

9. *Amend the HEA, or General Education Provisions Act, to* ***require that schools keep loan-related records for five years after the loan has been paid*** *in full and other Title IV-related records for five years after the last date of attendance.* This should include student attendance records which, in part, provide evidence of "satisfactory progress" for Title IV eligibility purposes.

10. In order to rank schools for program review and enforcement purposes, *create a* ***set of weighted, objective "risk factors"*** *based on the Department's experience with schools that have closed leaving funds owed to students and/or the Department*. We understand that this effort, consonant with Section 498A(a)(2) of the HEA, has been underway at the Department for some time. Congressional action requiring such a ranking, i.e. changing "may" in the statute to "shall", would ensure that it is implemented, rather than abandoned, in order to rationalize targeting of enforcement efforts.

11. ***Increase the use of unannounced visits*** *to suspect schools and* ***start using "shoppers"*** *to pose as prospective students where admissions fraud is suspected.* Neither of these measures would require new statutory authority. There is no better, and may be no other, way to prove unlawful activity than to surprise the perpetrators. Conversely,

advance notice allows unscrupulous schools to alter, hide or destroy key documents. Adelphi Business Schools, for example, became famous for their "moving libraries" which appeared on their campuses only when accreditors or regulators had announced planned visits. Also, shoppers have been used successfully by some state agencies to uncover or verify complaints, such as those involving falsified ability to benefit testing.

12. ***Maintain the existing caps*** *(no more than 50% of institution's courses of study may be correspondence or 50% of its students may be enrolled in correspondence courses)* ***for correspondence programs.*** *Ensure that they also cover "distance learning"; if any new institutional or programmatic eligibility waivers are created for distance learning, limit them t o non-profit schools.* Among the worst abuses of Title IV aid in the 1980's were those committed by proprietary correspondence schools. They recruited unqualified students, grossly inflated the clock hours their lessons represented, routinely created falsified ability to benefit and satisfactory progress records, often had withdrawal rates of 90% and more, and bilked students and taxpayers of millions of dollars. The special difficulties of measuring the quality of correspondence and other distance learning methods militates against allowing for-profit schools to obtain unlimited Title IV funds for such programs.

13. ***Maintain existing default cut-off provisions,*** the Department's most successful enforcement tool. Default cut-offs are responsible, in large measure, for the current reduction in student loan defaults.

We are also extremely concerned that the Department's stated goal of easing the regulatory burden on institutions may conflict with protecting students and with the Department's own enforcement capability. As the U.S. Senate Permanent Subcommittee on Investigations was told by the Department's Inspector General in 1995 during hearings on proprietary school abuses of the Pell Grant Program:

> *...it may be inviting to think that, in the context of reinventing government or otherwise, we can do away with prescriptive regulations. However, we must be cautious when applying this approach in an area or to an industry where there is an identified abuse of taxpayer funds and students.... [The] easy availability of huge sums of Federal ... funds provides motivation for some unscrupulous program participants to look for gaps in the existing laws and regulations in order to enhance their own financial interest rather than that of the students or the public. In rendering their decisions, courts will require that regulatory or legislative requirements are clear, and we must ensure that such requirements exist to protect taxpayers and the intended beneficiaries of the [federal] programs.* Statement of John P. Higgins, Acting Inspector General, U.S. Department of

Education, to Senate Permanent Subcommittee on Investigations' Hearing on "Abuses in Federal Student Grant Programs and Proprietary School Abuses", July 12, 1995, p. 10 of written statement.

Unless executed with great precision and care, regulatory simplification combined with current federal down-sizing efforts could have a disastrous multiplier effect, crippling enforcement efforts and increasing loan defaults. The Comptroller General has expressed concern that the federal government "has insufficient accounting systems and managers to ensure that ... liabilities [owed to the government] are properly monitored." "U.S. Is Taking On Rising Loan Risk-- As liabilities mount, oversight wanes", article by Jeff Gerth of New York Times, from San Francisco Chronicle, February 22, 1996, p. A6. De-regulation of the 1980's, numerous reports have shown, allowed booming growth in federal programs, including student loans, without adequate oversight. The result: horrendous student loan default rates, due in large measure to unscrupulous training providers set up exclusively to cash-in on Title IV funding. The tools for preventing unlawful activity by postsecondary institutions must be maintained and strengthened in order to protect students and to prevent the student loan defaults that result from such activity.

We hope the Congress will agree with us that regulatory relief is appropriate only where the regulatory provisions do not provide meaningful protection for students or taxpayers. Some recent "simplifications" that have taken place and are still in progress have not necessarily followed that principle. For example:

-Electronic funds transfers (EFTs) hold the potential for making loan proceeds more quickly available to students and of reducing paperwork in the loan disbursement process. EFTs also, however, hold potential pitfalls for educational consumers. Over the past few years, when student advocates have raised concerns for example about the loss of student control over loan funds through the use of EFTs, Department and other officials in the student aid industry assured us that the borrower can always maintain control by notifying the school to send back all or part of the loan funds if the student does not enroll, withdraws or simply determines that he or she does not want the total loan amount. The recent Cash Management Regulation (Nov. 29, 1996) attempts to address this problem by allowing a student 14 days from the notice of crediting the student's account with EFT proceeds within which to cancel the loan disbursement. While this is a step in the right direction, we believe the time limit is too short.

-Master checks again simplify the paperwork for lenders and schools by allowing one check to be cut for multiple students' loans, but deprive students of the power of check endorsement. The use of master checks, rather than individual ones also raises questions about tracking individual disbursements.

-Single loan applications for subsidized and unsubsidized Staffords lack an adequate explanation of the differences between the two types of loans. This may cause students unknowingly to incur larger unsubsidized loan debts than they can reasonably repay.

- The period allowed for schools to hold loan proceeds has fo many schools become the normal delay in disbursing loan proceeds, i.e the ceiling has become the floor. This delay allows schools to collect interest on the loan funds, while denying students access to moneys needed for their living expenses. This practice is particularly offensive in the case of unsubsidized loans since the borrower pays interest on the funds while the school holds them.

- Line-of-credit proposals under discussion would also distance borrowers from the process, diminish borrower control over funds, and tend to foster high borrowing. This concept is fraught with dangers for students and for taxpayers in that uninformed borrowing and over-borrowing will lead to increased loan defaults.

- Record retention rule changes may directly harm the Department's ability to effectively enforce the HEA and regulations. Acceding to institutional complaints about accumulation of paper, the record retention requirements now state that schools must retain loan disbursement documents for only 3 years after the student's last date of attendance. A student may stop attending one school but move on to another, have several years of deferments, and not go into repayment until more than three years after attendance at the first school. Yet, loan disbursement records (e.g. payment to student for funds in excess of tuition, crediting to student's account or other charges) are often kept at the school.Three years from the last date of attendance is simply not long enough for principal balance disputes to surface and be addressed.

In summary, program integrity is an ongoing concern for students and taxpayers and must not be relegated to a secondary role. Any regulatory relief urged by postsecondary institutions, lenders, or others should not be undertaken unless a finding is made that it will not adversely affect student protections, the Department's and the Inspector General's enforcement efforts, and the federal fiscal interest.

B. <u>The lingering effects of trade school fraud and need for borrower redress</u>

The HEA has enabled countless low- and moderate-income individuals who otherwise would have been unable to do so to obtain high quality education and postsecondary training. In so doing, the HEA, like the GI Bill before it, has opened the door to the American dream for millions of Americans. Unfortunately, it has also slammed the door shut on hundreds of thousands of low-income Americans by allowing unscrupulous trade schools to flourish and to hoodwink those most desperate for self-improvement into obligating themselves for loans to pay for worthless job training. The tragic result is students left with little or no training, no jobs, substantial debts they cannot possibly repay, ruined credit ratings, and ineligibility for further student aid to get a real education or high quality training.

Certain provisions in the 1992 amendments to the HEA, notably the closed school and false certification discharge provisions, provided relief to <u>some</u> of those victimized by unlawful or unethical trade school activity. We strongly support those provisions and urge no modification to them. What is called for is implementation by the Department and the guaranty agencies to effectuate the beneficent purpose of the discharge provisions. We have strongly urged the Department to work with us on a public service information campaign to ensure that all eligible students are reached and receive the loan cancellation to which they are statutorily entitled. Anecdotal evidence suggests that: (1) a large percentage of the defaulted borrowers eligible for closed school discharge have been unreachable due to inaccurate addresses in the hands of loan holders; and (2) only about 20% of the defaulted borrowers identified by guarantors as potentially eligible for closed school discharge and to whom notices of discharge rights have been sent even respond. Clearly, more needs to be done to reach out to these borrowers whose loans may go back as far as 1986 and who, therefore, otherwise may be lost to the system.

Furthermore, the 1992 provisions reach only a small segment of those who have suffered set backs from their experience with fraudulent trade schools. We believe that the Department already has sufficient statutory authority to cease collection of student loan balances owed by students whose school owes but failed to pay loan refunds on their behalf and then closed. The Department previously had indicated that it would by regulation provide relief to this group of students, but has not yet done so. We have strongly urged the Department to provide relief for these students by using its regulatory authority, or if deemed necessary, by seeking statutory authority.

<u>Recommendations (none of which require statutory amendments)</u>:

1. **Maintain, as written, the closed school and false certification discharge provisions** and implement them fully.

2. Encourage the Department to **embark on a public education campaign**, including public service announcements, working with students' advocates **to inform borrowers of their discharge rights.**

3. Encourage the Department to **step up recoupment activity against closed schools**, their principals and affiliates.

4. Urge the Department to **discharge loan balances**-- both prospectively for new loans and retroactively for existing balances-- **for students whose schoo owed but never paid loan refunds** on their behalf and which have closed.

C. Improving information available to students in order to reduce bad choices and consequent loan defaults

The availability of comparative consumer information on training programs may not save all prospective students from poor educational experiences. Unsophisticated and poor people desperate to better their situation may instead succumb to high pressure sales tactics. Nevertheless, without basic, comparative data it is impossible for consumers to make informed choices. Essential information for trade school students includes graduation rates; licensing examination pass rates, if applicable; and placement rates, showing the number of graduates who got the job for which they had trained (and not merely a "related job") within six months of graduation and who kept the job for at least four months. This information was required under prior Departmental regulations. We had urged such expanded information In our comments on the Right-to-Know Act regulations. We, again, strongly recommend that such data-- verified for accuracy-- be provided to prospective students and be compiled for distribution on a comparative basis by the Department.

Many other sources of information on schools should also be made available through the Department to students and their human services counselors and advocates. For example, we have strongly urged the Department to continue developing the Postsecondary Education Participants System (PEPS) to encompass data from all Departmental sources, accreditors, and state agencies and make this information accessible to the public, perhaps electronically. The National Student Loan Data System (NSLDS), already up and running and accessible by institutions, should also be available to students in order to help them track their loans and other aid. In order to be truly useful to all parties, of course, NSLDS information must be fully accurate and up-to-date-- two features we understand it cannot currently boast.

Regarding deferments, a confusing array of possibilities exist for borrowers depending on when their loan promissory notes were signed and when the proceeds were disbursed. The only statutory requirement for notification of deferment rights is that they be contained in the promissory note. Borrowers are often unaware of these rights. Thus, some entitled to postponement of the repayment obligation may unwittingly slip into default. More meaningful notice of deferment rights-- after leaving school-- should be given.

Recommendations:

1. Amend the HEA to **require schools that predominantly provide vocational training programs to provide**, in a uniform format, **data on their graduation, placement (as defined above), and licensure exam pass rates**. Vocational training institutions already retain the responsibility to compile the data under many state licensing laws and accrediting body standards. The statute should require that they provide the data to prospective students and to the Department. The Department would compile the data in comparative format for dissemination to the public. By including programs offered by both proprietary and non-proprietary institutions, prospective students will be able to engage in much more comprehensive comparison shopping. The data should be verified by some outside source, such as attestation by a certified public accountant, and should remain auditable by government entities.

2. **Make development of PEPS**, as a thorough data base, **a priority** to carry out the mandate of section 498A(a)(3) of the HEA and amend the statute to clarify public access to the data.

3. **Urge the Department to ensure that students have access to accurate, up-to-date NSLDS** data on their own student aid. This would enable students and their advocates to locate the holders of their student loans far more easily than can be accomplished currently. This would not require a statutory amendment.

4. Amend the statute to **require lenders or guarantors**, or the Department in the case of the Direct Loan Program, **to notify borrowers of their deferment rights** and to make deferments retroactive to the date of delinquency upon the borrower's showing that he would have been so entitled had he timely applied.

D. Increased funding for Adult Literacy Training

We know that the President is concerned with literacy issues and has proposed the use of volunteer literacy tutors and work study student tutors, a worthwhile endeavor which we support. But in order to make significant headway in the war against illiteracy, funds must be committed to provide the expertise of trained reading instructors both for students and to train lay tutors. The adult population, an increasing percentage of those seeking higher education and job training, is especially hard to reach and yet must not be forsaken.

Recommendation: We suggest that our national education policy should aim to raise literacy levels and increase the percentage of those with high school diplomas and equivalencies rather than allowing to grow the number of ATB students receiving aid meant for those in higher education. We strongly urge the Congress to allocate increased funds for localities under the Adult Literacy Act and to embark on a national adult literacy campaign.

E. Massive confusion in the student loan programs warrants an ombudsman program for student loan problems as a means for default avoidance

Some student advocates spend much of their work life trying to help students sort out complicated student loan problems like the following that never should have happened:

*a lump sum loan payment rather than delay the next payment date as intended, mistakenly hurled the borrower into default;

*a deferment granted on 5 of the student's 6 loans held by the same entity erroneously was not granted on the sixth and put the student into default, collection fees, and ineligibility for further aid to finish her last semester;

* a student whose Direct Loan is promptly, electronically received by the college can't get the excess proceeds for weeks because the college is holding them for the maximum allowable period-- although the student needs the loan proceeds for food and is accruing interest charges on the unsubsidized portion of the loan on which is earning interest.

Students trying to pay their loans and avoid default are increasingly tripped up by computer glitches, lost mail , and other administrative problems that are virtually impossible to untangle. As *Smart Money Magazine* put it, such students "get caught up in a maelstrom of bureaucratic bumbling, computer systems gone wild, misplaced paperwork, and even thuggish collection agencies. It's a tale of borrowers-- and there are thousands of them-- who've had their lives disrupted or even been put into default because of a mistake by their loan servicer or guaranty agency." "Getting the Third Degree", by Devin Leonard, March 1996, p. 108.

Few lawyers or other advocates have expertise in student loan issues at all, let alone the detailed and frequently changing regulations and actors. An Ombudsman Program, properly funded and staffed and with enough independence to be a strong advocate for borrowers and not an apologist for any systemic or individual failings, could serve several important functions. It could resolve individual borrowers' loan problems, thereby reducing defaults, and track systemic patterns.

We note that the California Student Aid Commission and Texas Guaranty Agency each have new ombudsman offices. While these may serve a useful role for loans held by those agencies, many borrowers have loans guaranteed or held by multiple agencies, agencies that do not have ombudsman offices, or have loans held by the Department either because they are Direct Loans or are FFEL loans in default and assigned to the Department. We also note that the Department has recently established a toll-free Customer Support Branch Inquiry Service for financial aid professionals. Dear Colleague GEN-96-12. The stated purpose of the new hotline is to provide a means to "cut through the red tape", with a 3 day turn around for questions from financial aid administrators. If students are truly viewed as the number one customer of the financial aid programs, they should also be provided with a meaningful way to cut through student loan red tape in order to help them avoid defaults.

Recommendation: Create an independent Ombudsman Office for resolving student loan complaints. One successful model for an ombudsman program is found in the Older Americans Act, 20 USC 3058g. The Student Loan Ombudsman Office could be part of the Department of Education housed in Washington or in one or more of the regional offices. Or the Ombudsman function could be contracted out to non-profit groups meeting strict eligibility guidelines. One funding mechanism would be to impose on lenders and/or guarantors, the parties seeking to perpetuate the complex FFEL program, a small fee per loan guaranteed. This funding mechanism obviously would require a legislative amendment.

F. Increasing Pell Grants and Structuring Tax Credit Proposals to Help the Poor

Low-income students who 20 years ago would have relied solely on grants today are highly dependent upon student loans due to the skyrocketing costs of higher education and the stagnation of federal grant monies. The dramatic imbalance between federal grants and loans is evidenced by the fact that while such grants as a percentage of all sources of aid doubled from 1963 to 1973, they have dropped steadily since then. In 1993, federal grants comprised less of the total than in 1963, i.e. less than 20% of all aid. The College Board, *Trends in Student Aid 1984 to 1994*. Federally backed student loans, on the other hand, have mushroomed in significance from roughly 20% of all aid in 1963 (equal to federal grants at the time) to over 50% of all aid in 1993. Id. Increasing the Pell Grant is the most direct and effective way begin to address the imbalance and to make higher education and training accessible to the poor. We, therefore, strongly support the President's proposal to increase the maximum Pell Grant to $3000. We recognize that this is a budgetary issue rather than a matter for reauthorization since the HEA already provides an even higher maximum than that proposed to be funded. Nonetheless, we wanted to get on record our support for this method of helping the poor.

While helpful for middle-income students, the tax credit proposals present a far less effective way to make higher education accessible to the poor. From the perspective of low-income students, we note three flaws in the proposals under discussion: (1) Unless the credit is refundable and applicable to very low levels of adjusted gross income it will not put any dollars in the pockets of people earning less than 150% to 200% of the poverty level; (2) Getting a $1500 tax credit in April will not enable those with no discretionary income to pay community college tuition for the previous September or January; and (3) Reducing any tax credits by the amount of federal grants received would cancel out rather than enhance the benefit.

The refundability issue is critical to the millions of individuals who have relied, in part or solely, on welfare for income support prior to the 1996 changes in federal law. While many of those individuals have some amount of earned income each year, typically it would be an amount well below the minimum income to incur a positive tax liability, especially after taking into account the Earned Income Tax Credit (EITC). It would indeed be ironic if the EITC, part of the effort to "make work pay", prevented low-income workers from receiving money for their education through the new education tax credit. Like the EITC, the education tax credit formula should, therefore, allow workers with any amount of earned income to receive some refundable credit, and should be phased out at higher levels of income.

The delayed reimbursement issue is not readily solved. If at all possible, the education tax credit should be eligible for the advance payment system that we understand is now allowed for the EITC (by having employer withholding reduced). That way, at least some low-income beneficiaries of the credit would get help with living expenses, while perhaps relying on Pell grants or other sources to pay for tuition and books.

Recommendations:

1. We strongly urge the Congress to **focus** its efforts **on increasing the Pell Grant** through the budget process.
2. If tax credits are to be considered, a **refundable tax credit** that would kick in at low income levels could help realize the worthy goal of putting community college within the reach of every American.
3. Any **tax credits should not be reduced by the amount of federal grants** received, or they truly will be of no help to low-income persons.

G. Providing labor market information to Title IV applicants and considering labor market needs in determining eligibility for Title IV aid to proprietary school vocational programs.

Current law requires that to attain eligibility for Title IV aid proprietary schools must provide "training to prepare students for gainful employment in a recognized occupation." Section 481(b)(1) of the HEA, 20 USC section1088(b)(1). Yet, as the GAO has recently pointed out, schools are not required to consider students' likelihood of securing employment in the occupation for which they were trained. Testimony before Subcommittee on Human Resources and Intergovernmental Relations, Committee on Reform and Oversight, House of Representatives, by Cornelia M. Blanchette, June 6, 1996, GAO/T-HEHS-96-158, pp. 11-12. In its 1991 report on abuses in Title IV programs, the Senate Permanent Subcommittee on Investigations had recommended that Congress:

> consider the feasibility of setting reasonable limits on the type of proprietary school education that federal dollars should subsidize, emphasizing

education and training from which students, and ultimately, society as a whole, will realistically benefit. In the past federal financing for relatively worthless training in "glutted" career fields has created unnecessary financial costs to the taxpayer and very real costs to the students in terms of lost opportunities in marketable skills. "Abuses in Federal Student Aid Programs," Report of the Senate Permanent Subcommittee on Investigations, Committee on Governmental Affairs, May 17, 1991, p. 35.

The Department's Inspector General, examining Title IV expenditures on one vocation, similarly noted that although approximately $725 million in Title IV funds are spent annually to train cosmetologists, the supply of cosmetologists routinely far exceeds the demand. In 1990, for example, over 113,000 students who enrolled in cosmetology programs did not obtain a license to practice. Office of Inspector General Management Improvement Report No. 93-03, March 12, 1993, p. 5. The Inspector General's Office concluded that, "students and taxpayers lose under this system...The Federal Government does no service to students by making Title IV funds available to them for vocational training if they do not eventually find gainful employment." Id., p. 1. Both the Inspector General and the Senate Permanent Subcommittee have suggested that labor market information be used to identify occupations where workers are needed, and to place reasonable limitations on Title IV funds to proprietary school training to fields in which demand exists. The GAO also apparently is studying this issue. See GAO/T-HEHS-96-158.

Recommendations:

1. As a start, the Congress should **require the Department of Education, in cooperation with the Department of Labor, to develop and make widely available to Title IV applicants accurate information on current and future market needs** for those trades and skills that are subsidized through federal student aid programs. For more sophisticated students, this information alone could diminish the likelihood of enrollment in programs offering training for glutted fields.

2. For less sophisticated educational consumers, however, more than information is needed. The HEA **definition of an eligible "proprietary school" should be amended to require such schools to provide evidence that each program for which they seek Title IV eligibility provides a reasonable chance that its students will find gainful employment** in the job for which they will be trained. This could be proven by a formula of verified completion and job placement and earnings data.

H. Ensure inclusion of legal organizations representing low-income students and other student organizations in future negotiated rulemaking or other negotiations with the Department

In the 1992 amendments to the HEA, Congress required the Department to convene regional meetings to obtain public involvement by affected parties in the development of proposed regulations and to conduct negotiated rulemaking on the regulations implementing the 1992 amendments. Section 492 of the HEA. The statute recognized that organizations representing students had an important role to play as representatives of parties directly affected by the amendments and specifically named " students" and "legal organizations that represent students" as those to be included. Section 492(a)(1).

The undersigned organizations were selected by the Secretary to participate in negotiations and did so over a period of 3 years. We feel that we made a significant contribution to the process and to the resulting regulations and also learned a great deal. The expertise we acquired should be tapped if the Department is directed by Congress to engage in negotiated rulemaking or other meetings with the higher education community. Inclusion of legal organizations representing students and other student organizations should, therefore, be made explicit in any new or continuing legislative provisions for processes between the department and the higher education community.

Thank you for this opportunity to comment. As noted above, we intend to provide specific statutory language for our proposals at a later date. We look forward to working with you to improve students' access to high quality education and training programs under the Higher Education Act. We also ask to be invited to participate in any future hearings by your Committee and the Subcommittee on Postsecondary Education, Training, and Life-Long Learning .

Very truly yours,

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John Head

- Cordling rushing for advisory consensus program..

- Conflicts of interest — Banks agree that its fed. money but GAs now are in services = more conflict
- 'complexity issue'

USAO - array of businesses - self destructing?

'EASI can make ... as simple as DL
Cordling: 'circle the wagons — do nothing'
→ get some discussion going.

- $8 billion ?

- ... → lender pay fees directly to GAs.

- ... - ... — "a state-run program"

- Great lakes - depends on smooth contractor relationships.
But lender-holders prefer GAs to have a bright line test in case of disagreement.

- Mayberry, jalors

- Training
- Geography of schools

- NSC 183 - not end of a move toward EASI.
contract

- Anecdote - Serv contract
AAT the most expensive, qual. bidder
AFSA was $30 mill. below, tech. same

- There will be fun instability in the system.

Essen for:
Lefforeds
Wildee / McKean

- EASI
neutral benefits buying as adviser for same?
like the stock exchange

Overview
more

- 50-128 [illegible] pts in [illegible]

Student Loan Options
Possible Settlement--Option 1b

		1998	1999	2000	2001	2002	98-02
Students							
Reduce DL student fees from 4% to 3%	BA	68	165	185	196	209	823
	O	36	112	157	170	181	656
Eliminate 1% guaranty agency insurance fee (non-add)	BA	93	172	178	196	207	846
	O	50	127	159	171	183	690
Reduce DL student fees additional 1% for Stafford	BA	39	92	102	108	113	454
	O	21	64	89	95	101	370
Reduce FFEL student fees 1% for Stafford	BA	55	96	100	107	111	469
	O	30	72	89	95	100	386
Students BA		161	353	387	411	433	1,745
Students O		87	248	335	360	382	1,412
GAs (including reserves)							
Increase default reinsurance payment to 100%	BA	106	101	102	109	114	532
	O	64	94	93	97	103	451
Eliminate SPCA	BA	(73)	(11)	(12)	(11)	(12)	(119)
	O	(69)	(10)	(10)	(10)	(11)	(110)
Reduce default retention from 27% to 18.5%	BA	(321)	(40)	(42)	(45)	(47)	(495)
	O	(302)	(37)	(37)	(39)	(42)	(457)
Net Return of Agency Reserves	BA	(731)	(127)	(186)	(186)	(1,271)	(2,502)
	O	(731)	(127)	(186)	(186)	(1,271)	(2,502)
GA BA		(1,019)	(77)	(138)	(133)	(1,216)	(2,584)
GA O		(1,038)	(80)	(140)	(138)	(1,221)	(2,618)
Banks and Secondary Markets							
Reduce guarantee to 95%	BA	(87)	(83)	(85)	(90)	(95)	(440)
	O	(52)	(77)	(77)	(81)	(85)	(372)
Flexible repayment options required	BA	(77)	(72)	(64)	(65)	(71)	(349)
	O	(53)	(68)	(62)	(60)	(64)	(307)
Sallie Mae fee on securitized loans	BA	0	(6)	(18)	(29)	(39)	(92)
	O	0	(6)	(18)	(29)	(39)	(92)
Set in-school interest rate at the govt borrowing rate	BA	(394)	(207)	(213)	(224)	(236)	(1,274)
	O	(216)	(255)	(191)	(200)	(211)	(1,073)
Banks and Secondary Markets BA		(558)	(368)	(380)	(408)	(441)	(2,155)
Banks and Secondary Markets O		(321)	(406)	(348)	(370)	(399)	(1,844)
Other							
Section 458 Savings	BA	(218)	(58)	(59)	(60)	(61)	(456)
	O	(113)	(107)	(75)	(68)	(61)	(424)
Interactive changes (FFEL)	BA	(12)	(5)	0	(3)	(2)	(22)
	O	(7)	(3)	3	6	5	4
Other BA		(230)	(63)	(59)	(63)	(63)	(478)
Other O		(120)	(110)	(72)	(62)	(56)	(420)
Total Federal BA		(1,646)	(155)	(190)	(193)	(1,287)	(3,472)
Total Federal O		(1,392)	(349)	(225)	(210)	(1,294)	(3,470)

	1998	1999	2000	2001	2002	98-02
Total FFEL BA	(803)	(227)	(232)	(251)	(277)	(1,790)
Total FFEL O	(605)	(291)	(210)	(222)	(244)	(1,572)
Recall GA Reserves BA	(731)	(127)	(186)	(186)	(1,271)	(2,502)
Recall GA Reserves O	(731)	(127)	(186)	(186)	(1,271)	(2,502)
Total DL BA	106	257	287	304	322	1,276
Total DL O	57	177	246	266	282	1,028
Section 458 Reduction BA	(218)	(58)	(59)	(60)	(61)	(456)
Section 458 Reduction O	(113)	(107)	(75)	(68)	(61)	(424)
Total BA	(1,646)	(155)	(190)	(193)	(1,287)	(3,472)
Total O	(1,392)	(348)	(225)	(210)	(1,294)	(3,470)

1/8/97 ($ in millions) Budget Service

Section 458 Spending -- FY 1997-1998
(In millions of dollars)

	1997	1998	Change	%Change
ACAs	$153	$152	-$1	-1%
PC&B	32	34	2	6%
Postage	12	14	2	17%
Rent	5	5	0	0%
Communications	1	1	0	0%
Travel	3	3	0	0%
Contracts				
ADP	258	295	37	14%
Non-ADP	11	11	0	0%
Interagency Agreements	5	5	0	0%
Printing	7	8	1	14%
Training	2	2	0	0%
Equipment and Supplies	2	2	0	0%
Total	$491	$532	$41	8%

1/3/98
Budget Service

Sec. 458

Direct Loans + Student Aid Management Costs	1,996 Estimate	1,997 Estimate	1,998 Estimate	1,999 Estimate	2,000 Estimate	2,001 Estimate	2,002 Estimate
Office of Postsecondary Education:							
OPE Payroll (with overtime and awards)	27,197,430	30,474,120	32,778,392	33,696,187	34,639,680	35,609,591	36,606,660
Subtotal, Personnel Expenses	27,197,430	30,474,120	32,778,392	33,696,187	34,639,680	35,609,591	36,606,660
Travel	1,572,000	2,982,000	3,059,532	4,099,896	4,206,493	4,315,862	4,428,075
Printing	6,733,000	7.333,000	7,523,658	8,618,400	8,842,478	9,072,383	9,308,265
Non-ADP /A&A/ Purchases from govt	14,290,000	15,400,000	15,641,000	16,047,666	16,464,905	16,892,993	17,332,211
Automatic Data Processing (ADP) Contracts:							
DL Origination/Servicing	89,230,000	136,181,000	169,827,000	243,884,000	321,491,000	422,084,000	503,347,000
Other ADP Contracts	99,788,000	114,397.960	118,642,791	120,769,808	136,791,998	127,058,342	131,661,387
Contractual Modifications							
Training	989,000	2,111,285	2,200,000	2,257,200	2,315,887	2,376,100	2,437,879
Equipment and Supplies	248,000	636,000	706,000	724,356	743,189	762,512	782,337
ADP Equipment	901,000	885,000	910,000	933,660	957,935	982,841	1,008,395
Administrative Expense Allowances	166,868,000	152,751,920	152,142,595	147,984,928	147,207,467	153,859,914	163,585,343
Subtotal, Non-personnel Expenses	380,619,000	432,678,165	470,652,576	545,319,914	639,021,354	737,404,948	833,890,892
Subtotal, Costs (OPE)	407,816,430	463,152,285	503,430,968	579,016,101	673,661,034	773,014,539	870,497,551
Other Offices (Central Svcs, Utilities, Other Overhead):							
Payroll for Other Offices (With Overtime & Awards)	2,005,000	1,952,533	1,003,077	2,552,511	2,590,251	2,652,558	2,716,610
Non-Personnel Costs (includes central costs such as rent)	24.864,000	25,895,182	27,565,955	28,431.388	28,748,715	30,332,903	30,785,839
Subtotal, Costs (Other Offices)	26,869,000	27,847,715	28,569,032	30,983,900	31,338,966	32,985,461	33,502,449
Total, Direct Loans + Student Aid Management Costs	434,685,430	491,000,000	532,000,000	610,000,000	705,000,000	806,000,000	904,000,000
unobligated balance, end of year	314,570	0	0	-0	0	-0	-0
appropriation	435,000,000	491.000,000	532,000,000	610,000,000	705,000,000	806,000.000	904,000,000

Student Aid Automated Data Processing Contract Costs -- FY 1997-98

(In millions of dollars)

	Section 458 Funds				All Funding Sources			
	1997	1998	Change	%Change	1997	1998	Change	%Change
Direct Loan Servicing	$116	$146	$30	26%	$116	$146	$30	26%
Direct Loan Origination	20	23	3	15%	20	23	3	15%
Subtotal, Servicing and Origination	136	169	33	24%	$136	$169	33	24%
Central Processing System	23	23	0	0%	24	24	0	0%
Multiple Data Entry	22	22	0	0%	28	27	-1	-4%
National Student Loan Data System	27	32	5	19%	27	32	5	19%
Public Inquiry Contract	13	14	1	8%	13	15	2	15%
Stafford/Perkins Data Systems[1]	2	3	1	50%	18	21	3	17%
Subtotal, Volume-Driven Contracts	223	263	40	18%	246	288	42	17%
Tile IV Wide-Area Network	17	17	0	0%	18	18	0	0%
Others	18	15	-3	-17%	36	34	-2	-6%
Total	$258	$295	$37	14%	$300	$340	$40	13%

[1]Total excludes default collection-related activities that are funded in the FFEL subsidy.

1/10/98
Budget Service

75% of all contracts

ADP Contracts

Contract Name	1997 Current Estimate Total	PA	FFEL	458	FY 1998 Total	PA	FFEL	458	FY 1999 Total	PA	FFEL	458
Volume Driven Contracts												
Multiple Data Entry	27,800	5,318	0	22,482	27,130	5,190	0	21,940	27,820	5,322	0	22,498
Stafford Perkins Data Services	17,500	4,646	10,474	2,380	20,560	5,459	12,305	2,796	22,610	6,003	13,532	3,075
National Student Loan Data System	27,055	0	0	27,055	31,600	0	0	31,600	33,650	0	0	33,650
Central Processing System	24,210	484	484	23,242	23,910	478	478	22,954	24,150	483	483	23,184
Direct Loan Origination/Servicing	136,181	0	0	136,181	169,827	0	0	169,827 →	243,884	0	0	243,884
Public Inquiry	13,430	672	0	12,759	14,900	745	0	14,155	15,590	780	0	14,811
Subtotal, Volume-Driven Contracts	246,176	11,120	10,958	224,098	287,927	11,872	12,783	263,272	367,704	12,587	14,015	341,101
Non-Volume Driven Contracts												
Campus Based Maintenance & Operations	1,730	1,730	0	0	1,858	1,858	0	0	1,906	1,906	0	0
Central ADP Costs (CIO)	6,390	1,807	1,462	3,121	6,669	1,856	1,536	3,277	6,842	1,904	1,576	3,362
Direct Loan Model Development (PPI)	450	0	0	450	450	0	0	450	450	0	0	450
DL MIS Initial Development	0	0	0	0	200	0	0	200	205	0	0	205
EASI/ISAMS	5,000	0	0	5,000	5,000	0	0	5,000	2,840	0	0	2,840
ED Payment Management System	150	0	0	150	150	0	0	150	154	0	0	154
Electronic Archiving/Optical Imaging	300	0	0	300	300	0	0	300	308	0	0	308
GA Quality Control Project	206	0	0	206	200	0	0	200	205	0	0	205
Institutional Quality Control Assurance	710	480	0	230	710	480	0	230	728	492	0	236
Litigation Support Preparation	151	5	0	146	150	5	0	145	154	5	0	149
Lotus Notes Support	500	0	0	500	500	0	0	500	513	0	0	513
OCFO Accounting System Support	1,638	0	0	1,638	1,720	0	0	1,720	1,765	0	0	1,765
OHEP Management System	250	250	0	0	200	200	0	0	205	205	0	0
OPE Program/Management Analysis	641	280	0	361	610	280	0	330	626	287	0	339
OUS DL Evaluation	1,338	0	0	1,338	1,338	0	0	1,338	1,338	0	0	1,338
OUS Program Cost Estimation Support	400	0	0	400	420	0	0	420	431	0	0	431
Pell Cost Estimating Model	275	275	0	0	300	300	0	0	308	308	0	0
Pell Recipient Management Information	11,032	11,032	0	0	10,821	10,821	0	0	11,102	11,102	0	0
Postsecondary Ed Participants System	3,406	1,958	0	1,448	2,472	1,958	0	514	2,536	2,009	0	527
System Security Reviews	250	100	0	150	250	100	0	150	257	103	0	154
Title IV Financial Analysis	51	10	0	41	0	0	0	0	0	0	0	0
Title IV System Technical Support	525	250	0	275	400	250	0	150	411	257	0	154
Title IV Wide Area Network	18,000	776	0	17,224	17,655	776	0	16,879	18,114	796	0	17,318
Total	299,569	30,073	12,420	257,076	340,300	30,756	14,319	295,225	419,102	31,961	15,591	371,550

Contract Name	FY 2000 Total	PA	FFEL	458	FY 2001 Total	PA	FFEL	458	FY 2002 Total	PA	FFEL	458
Volume Driven Contracts												
Multiple Data Entry	33,740	5,498	0	28,242	29,660	5,674	0	23,986	30,810	5,894	0	24,916
Stafford Perkins Data Services	29,210	6,693	15,088	7,429	28,050	7,447	16,788	3,815	30,940	8,215	18,518	4,208
National Student Loan Data System	35,820	0	0	35,820	37,340	0	0	37,340	38,920	0	0	38,920
Central Processing System	29,540	491	491	28,558	24,900	498	498	23,904	25,300	506	506	24,288
Direct Loan Origination/Servicing	321,491	0	0	321,491	422,084	0	0	422,084	503,347	0	0	503,347
Public Inquiry	16,320	816	0	15,504	17,090	855	0	16,236	17,890	895	0	16,996
Subtotal, Volume-Driven Contracts	466,121	13,498	15,579	437,044	559,124	14,474	17,286	527,364	647,207	15,509	19,024	612,674
Non-Volume Driven Contracts												
Campus Based Maintenance & Operations	1,956	1,956	0	0	2,007	2,007	0	0	2,059	2,059	0	0
Central ADP Costs (CIO)	7,021	1,954	1,617	3,450	7,203	2,005	1,659	3,539	7,390	2,057	1,702	3,631
Direct Loan Model Development (PPI)	450	0	0	450	450	0	0	450	450	0	0	450
DL MIS Initial Development	211	0	0	211	216	0	0	216	222	0	0	222
EASI/ISAMS	0	0	0	0	0	0	0	0	0	0	0	0
ED Payment Management System	158	0	0	158	162	0	0	162	166	0	0	166
Electronic Archiving/Optical Imaging	316	0	0	316	324	0	0	324	332	0	0	332
GA Quality Control Project	211	0	0	211	216	0	0	216	222	0	0	222
Institutional Quality Control Assurance	747	505	0	242	766	518	0	248	787	532	0	255
Litigation Support Preparation	158	5	0	153	163	6	0	157	167	6	0	161
Lotus Notes Support	526	0	0	526	540	0	0	540	554	0	0	554
OCFO Accounting System Support	1,811	0	0	1,811	1,858	0	0	1,858	1,906	0	0	1,906
OHEP Management System	211	211	0	0	216	216	0	0	222	222	0	0
OPE Program/Management Analysis	642	295	0	347	658	302	0	356	676	310	0	366
OUS DL Evaluation	1,338	0	0	1,338	1,338	0	0	1,338	1,338	0	0	1,338
OUS Program Cost Estimation Support	442	0	0	442	454	0	0	454	465	0	0	465
Pell Cost Estimating Model	316	316	0	0	324	324	0	0	332	332	0	0
Pell Recipient Management Information	11,391	11,391	0	0	11,687	11,687	0	0	11,991	11,991	0	0
Postsecondary Ed Participants System	2,602	2,061	0	541	2,670	2,115	0	555	2,740	2,170	0	570
System Security Reviews	263	105	0	158	270	108	0	162	277	111	0	166
Title IV Financial Analysis	0	0	0	0	0	0	0	0	0	0	0	0
Title IV System Technical Support	421	263	0	158	432	270	0	162	443	277	0	166
Title IV Wide Area Network	18,585	817	0	17,768	19,068	838	0	18,230	19,564	860	0	18,704
Total	515,897	33,377	17,196	465,324	610,146	34,870	18,945	556,331	699,510	36,436	20,726	642,348

FY 1998 Student Aid Administration Funding Requirements
Justification of Estimates

Total costs in millions of dollars. Unit costs in whole dollars. No. of units as labeled.

Administrative Cost Allowances

		1996	1997	1998	1999	2000	2001	2002
		Total Costs						
		$166.9	$152 8	$152.1	$148.0	$147.2	$153.9	$163 6
Unit	Unit Cost	No. of Units (In billions)						
FFEL Consummated Volume	$0.0085	19.6	18.0	17.9	17.4	17.3	18.1	19 2

Budget estimates assume continuation of FY 1997 ACA policy of paying guaranty agencies .85 cents for each new dollar of new loan volume. (New loan volume is calculated exclusive of consolidations and unconsummated loans, i.e., those that are originated but never guaranteed.) Because ACA bills are submitted across two fiscal years, 40 percent of the totals for each year reflect prior year volume, and 60 percent reflect current year volume.

Personnel

	1996	1997	1998	1999	2000	2001	2002
	Total Costs						
	29.2	32.4	33.8	36.2	37 2	38 3	39.3
Unit	No. of Units (In whole numbers)						
FTE	481	520	520	520	520	520	520

These figures reflect expected needs for salaries and benefits for Department employees working on the student aid programs. FTE includes employees of the Office of Postsecondary Education and certain support office personnel. No increases in FTE over the FY 1997 level are anticipated. Cost increases after FY 1997 reflect government-wide assumptions for cost-of-living increases

Volume-Driven Contracts

Costs for these contracts vary depending on specific drivers. For most of these contracts, which involve both student loan and grant programs, these cost drivers are not directly tied to loan volume, but rather to items such as the number of applications for student aid. In addition to these variable costs, these contracts also include contract-mandated fixed costs for activities such as system maintenance, scheduled upgrades, management information reports, and quality control activities. These fixed costs increase by inflation and computer and processing upgrades

Direct Loan Origination/Servicing

	1996	1997	1998	1999	2000	2001	2002
	Total Costs						
Fixed	21.2	21.3	19.9	24.5	23.1	23 7	24.3
Variable - Origination	13 1	16.2	20.0	23.7	26 6	28 6	30.9
Start-up/Recompetition - Origination	--	7.2	--	--	--	10 0	--
Task Orders - Origination	--	3.4	--	--	--	--	--
Variable - Servicing	39.9	78.1	130 0	195.7	271.8	355.7	441 3
Start-up/Recompetition - Servicing	--	10 0	--	--	--	4.0	6.8
Total	74.2	136.2	169.9	243 9	321.5	422.0	503.3
Unit	No. of Units (In billions)						
No. of Loans Originated	2 6	3.2	3 9	4.5	4 9	5.2	5.4
No. of Loans Serviced	4.0	7.1	10 8	14.9	19.2	23 6	28 0
	Unit Costs						
~~No. of Loans~~ Originated	$5.08	$5.07	$5 11	$5 25	$5.39	$5 53	$5 68
~~No of Loans~~ Serviced	$9.99	$11 00	$12.08	$13 15	$14.13	$15.07	$15 76

Fixed costs include systems maintenance and improvements and contractor personnel. Variable origination costs increase as additional loans are originated and are primarily activities related to establishing the new loan in the contractor's system. Variable servicing costs are costs related to the number of loans in school, in deferment, and in repayment This last category, which generates the highest per unit costs, began to increase dramatically in FY 1996 as substantial numbers of students who took out loans in the first two years of the program started to enter repayment

EDS began originating consolidation loans in Fall 1996, and is expected to originate all new loans as of May 1997 Three new servicing contracts were awarded in Fall 1996 and are expected to begin servicing loans as of July 1, 1997.

Justification of FY 1998 Student Aid Administration Funding Requirements -- Cont.

Total costs in millions of dollars. Unit costs in whole dollars. No. of units as labeled.

National Student Loan Data System

	Total Costs						
	1996	1997	1998	1999	2000	2001	2002
Fixed	$6.1	$10.2	$14.0	$14.4	$15.1	$16.1	$16.9
Variable	15.4	16.8	17.6	19.3	20.7	21.3	22.0
Total	21.5	27.0	31.6	33 7	35.8	37.4	38.9

Unit	No. of Units (In millions)						
No. of Loans on System	74	89	93	102	112	121	132
	Unit Costs						
	$0 21	$0.19	$0 19	$0.19	$0 18	$0 18	$0.17

NSLDS maintains a data base of loan activity for all borrowers in both the FFEL and Direct Loan programs. This system is used to pre-screen applicants, identifying borrowers who are in default, have reached statutory loan limits, or are otherwise ineligible to receive new loans; calculates cohort default rates to determine institutional eligibility to participate in the loan programs; and provides detailed financial data for use in default management and research activities. As of July 1996, NSLDS also began providing schools with student financial aid transcripts.

Additional fixed costs in FY 1998 reflect increased costs associated with the competition for and award of a new contract to administer the data system.

Central Processing System

	Total Costs						
	1996	1997	1998	1999	2000	2001	2002
Fixed	12.6	14.3	14.3	14.3	14 3	14.3	14.3
Variable - New Applications	3.9	4.4	4.3	4.4	4.6	4.7	4.9
Variable - Renewal Applications	4.9	5.5	5.4	5.5	5.7	5.9	6 1
Recompetitions/Start-up	--	--	--	--	5.0	--	--
Operation March	3.0	--	--	--	--	--	--
Total	24.4	24.2	23.9	24.2	29.5	24.9	25 3

Unit	Unit Cost	No. of Units (In millions)						
No. of New Applications	$0.88	4.4	5 0	4 9	5.0	5.2	5.4	5 6
No of Renewal Applications	$0.86	5 7	6.4	6 2	6 4	6 6	6 9	7.1

The Central Processing System reviews applications for all Federal student financial assistance, determines student eligibility, and informs students, parents, and schools of loan and grant award levels.

Totals for FY 1996 includes $3 million in one-time costs for Operation March, under which the backlog of student financial aid applications for AY 1996-1997 was eliminated

Stafford/Perkins Data Systems

	Total Costs						
	1996	1997	1998	1999	2000	2001	2002
Fixed	7.1	10.1	11 1	11.7	12 3	12 9	13 5
Variable	17.3	17.4	19.4	20.9	23.0	25 2	27 4
Recompetitions/Start-up	--	--	--	--	4.0	--	--
Total	24.3	27.5	30 5	32.6	39.2	38 1	40 9

Unit	Unit Cost	No. of Units (In millions)						
No. of Defaulters	$1 20	14 4	15.6	16.2	17.5	19.1	21 0	22 9

This contract processes default claims from guaranty agencies and for schools in the Perkins Loan program. In addition, this contract is the Department's primary management tool for default prevention and collection activities. Increases in fixed costs in the FY 1998 estimate reflect improvements in computer and reporting systems which are expected to improve default collection activities.

Justification of FY 1998 Student Aid Administration Funding Requirements -- Cont.

Total costs in millions of dollars. Unit costs in whole dollars No of units as labeled.

Multiple Data Entry Contracts

	Total Costs						
	1996	1997	1998	1999	2000	2001	2002
Fixed	$1.6	$1.6	$1.6	$1 6	$1 6	$1.6	$1 6
Variable	22.3	26 2	25.5	26.2	27 1	28.1	29 2
Operation March	0.2	--	--	--	--	--	--
Recompetitions/Start-up	--	--	--	--	5.0	--	--
Total	24 1	27.8	27 1	27.8	33.7	29.7	30.8

Unit	Unit Cost	No. of Units (In millions)						
No. of Applications	$2.30	9.7	10.9	11.1	11.4	11.8	12.2	12.7

These contracts input data from applications for Federal student financial aid into the central processing system. Increase in variable costs reflect projected growth in the number of applications for Federal financial aid.

Public Information Contract

	Total Costs						
	1996	1997	1998	1999	2000	2001	2002
Fixed	1.6	1 2	2.1	2.1	2 2	2 2	2.3
Variable - Defaults	2.5	4.2	4.5	4.7	4.9	5 2	5.4
Variable - Non-Defaults	4 6	8.0	8.4	8 8	9.2	9.7	10.2
Total	8 7	13 4	14.9	15.6	16.3	17.1	17.9

Unit	Unit Cost	No. of Units						
		1996	1997	1998	1999	2000	2001	2002
No of Inquiries/Default	$2.84	0 9	1.5	1.6	1.6	1 7	1 8	1.9
No. of Inquiries/Non-Default	$2.84	1 6	2.8	3.0	3.1	3.3	3 4	3 6

This contract generates responses to written and phone inquiries involving Federal student financial assistance, including the status of defaulted loans. Both fixed and variable costs under this contract have increased due to a greater Department emphasis on upgrading customer service In addition, variable cost increases reflect projected growth in the number of inquiries

	1996	1997	1998	1999	2000	2001	2002
Subtotal, Volume-Driven Contracts	$177.3	$256.1	$298 0	$377.8	$476.1	$569.1	$657.1

Sally & Graham

- Comparison of our screening costs vs.
Sallie or other private scrn...

* Rolecaler - Tuition cap - equal share of new borrowers.
DL/Bergx etc.

- Ed/general / diff. loan. services.

1/8 - 21 servicer - (SCMA discussion)

* NSLDS - not nec. to screen students -
use CAVRS for $100K
- CPS also has the data.

- Paying GAs etc. by NSLDS data → how does that improve quality of the data?

- CPS

WORK
- tech.
- special ed.

National Direct Student Loan Coalition

"An Alliance of Schools Participating in the Federal Direct Student Loan Program"

LEVEL PLAYING FIELD PROPOSALS

MAKING LOAN PROGRAMS WORK FOR COLLEGE STUDENTS AND THEIR FAMILIES

The Student Loan Reform Act of 1993 set a new management paradigm for the Department of Education that should be enhanced. The National Direct Student Loan Coalition, a group of institutions participating in the Federal Direct Student Loan Program (FDSLP), supports the extension of these reforms to all federal student loan programs. The FDSLP involves more than 1600 schools and over one third of the federal student loan volume.

▪ **Benefits for All Borrowers** -- Currently FFELP guaranty agencies and lenders may use excess profits derived from federal subsidies to finance discounted origination fees and interest rates for some students. This indirect use of federal funds provides an unfair advantage for some students at the expense of others. These rates and benefits should be available to all borrowers. Any excess profits within the federal student loan programs should be redirected to equitably benefit all FDSLP and FFELP student borrowers.

▪ **Flexible Repayment for All** -- Borrowers should have the same flexible repayment options, regardless of the origin of their loan. Standard, extended, graduated, and income-contingent repayment options should be extended to students borrowing under FFELP. However, the borrower's right to change repayment plans, at no cost, must also be available to FFELP borrowers throughout the life of their loans. Lenders must agree to write off any loan balances remaining after 25 years for borrowers choosing income contingent repayment. Further, any balances cancelled after 25 years should be excluded from taxation under both programs.

▪ **Nondiscrimination** -- The federal government should offer all eligible students and their families the same promise of equal access to educational loans. Lenders must be required to lend to "all eligible students (and the eligible parents of such students) in attendance at participating institutions of higher education," as established by Section 451 of the Student Loan Reform Act of 1993. Currently, FFELP allows lenders to selectively choose the people and institutions who will have access to federally guaranteed loans and loan programs.

▪ **Consumer Oriented Loan Servicing** -- Simplicity is a proven concept of the Student Loan Reform Act of 1993 that can be extended to FFELP borrowers. FDSLP borrowers are assured that they will deal with one servicer for all their loans for the duration of their obligation. This "one lender/one holder/one guarantor rule" should be extended so that all borrowers of federally guaranteed loans are assured that their loans will never be sold without permission and that they will have one servicer with which to deal throughout the life of their loans.

▪ **Service, Delivery, and Simplicity** -- The FDSLP establishes high standards of service and delivery for borrowers which should be the standard for all federal student loan programs. The simplicity of the Free Application for Federal Student Aid (FAFSA) must be safeguarded.

▪ **Competition** – As long as the Congress authorizes two student loan programs, competition between the FDSLP and the Federal Family Education Loan Program (FFELP) fosters enhanced performance in FFELP that benefits both borrowers and their schools. Freedom of choice allows a school to choose the federal loan program that best serves its students. The removal of incentives for continuous improvement and further reform – either by arbitrarily capping Direct Loan volume or by conscripting schools into FDSLP – would undermine progress made by earlier student loan reform efforts.

▪ **Identical Budget Scoring Rules for Federal Student Loan Programs** – A fair and equitable comparison of taxpayer costs within the two federal student loan programs is critical. In action denounced by editorial boards across the nation, opponents of FDSLP required the Congressional Budget Office to include the administrative costs of the direct loan program, but not the FFEL program. Current law requiring all federal credit programs to include one year's worth of federal administrative costs in each annual budget should be applied identically to all federal student loan programs. Otherwise, taxpayers will not be able to evaluate the relative costs and merits of these two programs.

▪ **Accountability** – All federal loan programs should adhere to the consistent standards of quality and accountability established under the Student Loan Reform Act of 1993. Like their counterparts in FDSLP, schools choosing FFELP should be required to implement a quality assurance program. Further, all entities administering federal loan funds should be required to reconcile funds monthly, in accordance with the standards established by the Federal Student Loan Reform Act of 1993, to ensure proper management.

▪ **Integrity** – State guarantee agencies, lending institutions, state higher education agencies, and other organizations involved in FFELP should acknowledge their relationships and eliminate those areas in which the General Accounting Office (GAO) has identified conflicts of interest. Several state structures make it difficult, if not impossible, for those who want to join direct lending to do so. The U.S. Department of Education has no authority to conscript schools for FDSLP; consequently, there should be no coercion or state mandates to keep schools from joining direct lending.

▪ **Responsible Stewardship of Public Funds** – In order to maintain the integrity of the federal student aid programs, legislation and regulations should continue to be strengthened to safeguard taxpayer dollars. Cash and service donations to student aid associations (often from federal reserve funds), sponsored social and conference entertainment for such associations (including gifts and prizes) are not an appropriate use of funds derived from federal sources. Personal trips, golf outings, hospitality suites, and other private benefits should not be provided through the federal student loan programs. The public trust demands the high standards of stewardship established by the Student Loan Reform Act of 1993.

▪ **Aggressive Default Prevention and Loan Collection** – The Student Loan Reform Act of 1993 established aggressive default prevention/collections procedures. Responsible stewardship of taxpayer dollars requires that all entities involved in federal student loan programs reconcile funds monthly and that such information be electronically provided to the U.S. Department of Education. Now that FDSLP schools have proven that it is a workable approach, it can be extended to FFELP schools and lenders to ensure proper fiscal management of the FFELP.

12/13/96

Patricia A. Smith

12/19/96 04:24:04 PM

Record Type: Record

To: Robert M. Shireman/OMB/EOP

cc:

Subject: Re: We may need tonight

Outlay cost for each 1% reduction in orig. fee --

	98	99	00	01	02	total
FFEL						
Staff.	61	92	89	95	100	436
unsub.	32	52	54	58	63	258
PLUS	9	16	16	18	21	80
Total	102	160	159	171	183	774
Direct						
Staff.	42	78	89	96	101	406
unsub.	23	43	49	54	57	226
PLUS	8	15	19	21	23	86
Total	73	136	157	170	181	717

To reduce more than 1%, just multiply.

Staff only: 103 170 178 191 201 843

Robert M. Shireman
12/13/96 06:26:18 PM

Record Type: Record

To: Anita Chellaraj/OMB/EOP

cc: Barry White/OMB/EOP, Patricia A. Smith/OMB/EOP
Subject: Re: Student Loan savings estimates

Here is the ONE line of numbers that should appear for student loans:

Student loans:

98	99	00	01	02	total
-1379	-851	-804	-827	-1299	-5160

Yes, it keeps getting bigger. We keep finding additional ways of saving money.

Also, as I said on my voice mail message, change the word "establish" to "Improve" third grade literacy; and strike the "Increase" before school construction. Thanks.

DEPARTMENT OF EDUCATION
(outlays in millions of dollars)

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002
STUDENT LOANS:					
Appeal..................	-2542	192	245	253	263
Recommendation.......	-1379	-851	-804	-827	-1299

- **Reform design**: The passback called for the guaranty agencies to be eliminated, the guarantee function to be performed directly by the Department, and performance-based contracting to be used for the administration of the Federally guaranteed program. The Department objected primarily on political grounds: a radical proposal would stir up so much opposition that it would be counter-productive and would harm other education initiatives.

  The Department's appeal calls for continuation of the Secretary's existing authority to make "agreements" with intermediary agencies, rather than relying on competitive contracting, even though loans would be guaranteed directly by the Secretary. They propose modest financial incentives to improve lender and intermediary agency performance. Savings come primarily from the take-back of reserves and reductions in subsidies to lenders.

  The recommended approach would include the direct guarantee of loans by the Secretary, reforms of the financial incentives for lenders and intermediary agencies with whom the Secretary has agreements, strict performance requirements for intermediary agencies. It would accept the Secretary's political argument and not require performance-based contracting, but would provide clear authority for the Secretary to use contracts as necessary to manage the guaranteed loan program effectively. Reserve funds are taken back over the five-year period.

- **Borrower-paid fees**: The passback agreed with the Department's request to reduce student fees by one percentage point (from four percent to three percent), as part of an effort to equalize the terms of the Direct and guaranteed programs. The Department wants to go further, using much of the generated savings in order to eliminate the 3% fee for low- and moderate-income students (those in the subsidized Stafford program). The Department argues that the further reduction is needed in order to do battle with Republican fee-reduction efforts. The recommendation would not reduce fees further.

- **Five-year savings**: The appeal results in five-year outlay savings of -1590. The recommendation results in five-year outlay savings of -5160.

Patricia A. Smith

12/19/96 04:24:04 PM

Record Type: Record

To: Robert M. Shireman/OMB/EOP

cc:

Subject: Re: We may need tonight

Outlay cost for each 1% reduction in orig. fee --

	98	99	00	01	02	total
FFEL						
Staff.	61	92	89	95	100	436
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unsub.	23	43	49	54	57	226
PLUS	8	15	19	21	23	86
Total	73	136	157	170	181	717

To reduce more than 1%, just multiply.

11/26/96

Ex. Loans w/ Raines

☐ where the come back?

- Moodys / S&P - steadily [illegible]

bonds . . .

☐

check

- '98 - reserves

- FISC

+ same [illegible] in their [illegible] direction . . .

☐

Problem ?

→ same default risk as [illegible] GSL

well managed = 2% TARGET of some sort

→ 14 % . . .

- then they decide when to make a phone call, etc.

- Servicing shd be in the calculation
(at a minimum)

- $6 billion add-on to deficit (outlays)

(in Disc. → outlays to a financing account)

- Markets "same money" = when the rate Δs...
- one of the purp. in the index change.

⇒ need to talk abt effects...
(incl. effect on the '98 rate!)

- Floor - fix it...
windfall -

- Bid the rate

'Don't contract, just do it directly...'

PREPARER/EXT: Pat Smith/5-5882

Department of Education
(In millions of dollars)

ISSUE: **Student loans (Federal Family Education Loans and Federal Direct Student Loans)**

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	Total
Midsession Baseline OL..................... (Subject to new economics and technicals)	2,898	3,052	3,269	3,469	3,681	16,117
Option 1: FY 1997 Budget, revised.	-1,046	-519	-486	-486	-495	-3,031

Note: these savings are being carried in the preliminary FY 1998 Budget plan.

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	Total
Option 2: Agency request	-2,653	9	73	80	81	-2,411

The agency request is to reduce borrower fees, lender yield, and Federal administrative costs, require lenders to offer income-contingent repayment and pay for loan amounts not repaid, and restructure guaranty agencies. ED's proposed savings include the savings in option 1. If those savings are assumed to be already part of Administration policy, ED's proposal costs $.6 billion.

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	Total
Option 3: PAD alternative	-1,459	-762	-701	-714	-731	-4,367

Reduce lender yield and Federal administrative costs as in option 1. Reduce borrower fees by a lesser amount than the agency proposal, and offset the cost with a further reduction in lender yield. Replace guaranty agencies with contractors in the guaranteed program. If the savings in option 1 are assumed to be already part of Administration policy, the PAD alternative saves an additional $1.3 billion.

DESCRIPTION OF ISSUE: In 1993, the President proposed to "scrap" the guaranteed student loan system and replace it with one that was simpler for schools and families, cheaper for taxpayers, and offered students the option of paying off their loans as a small percentage of their income after they graduate. Congress, in the 1993 reconciliation bill, provided for a partial phase-in of the new Direct Student Loan Program, but punted on the question of the ultimate fate of the guarantee system (the Federal Family Education Loan Program, or FFELP). During the negotiations over the final bill, Secretary Riley expressed concern that in failing to completely reform the system, the lenders and guaranty agencies would keep coming back and could even undermine direct lending.

When the Republicans took over Congress after the 1994 election, the Direct Loan Program was still in its infancy, with only five percent of total loan volume. But the schools and students were thrilled with the improvements that the new system offered. In order to protect the program from elimination or caps, the Administration shifted from a policy that assumed a phase-out of FFEL, to one that promoted competition -- allowing schools to decide which program they want to deliver loans to students at their institutions. Students do not have a choice, except that they can consolidate their FFEL loans in to direct lending if their lender does not offer a satisfactory repayment plan, including income-contingent repayment.

Despite the controversy in Congress, the Direct Loan Program grew to 31 percent of loan volume in its second year, 1995-96. That was below the target of 40 percent, but the same as the phase-in target that the President had originally proposed. While the rave reviews of the program continued, this year it grew to only 35 percent (and three/fourths of the new schools are small trade schools). Despite minimal public notification, over 100,000 FFEL borrowers have consolidated into the direct loan program.

There are three primary reasons that growth of the Direct Loan Program has slowed. First, in a "choice" environment, the ones who most wanted to leave FFEL did so in the first and second year. For the many schools that had been toying with the idea of entering the program's third year, the debate in Congress prompted them to sit tight. Second, competition from direct lending has improved the guarantee program. As a result, many institutions support the continuation of both programs in order to continue the trend of improvements in the bank-based program and the quality of direct lending.

Finally, for the first time in the 30-year history of the guarantee program, some of the participants have discovered price competition, albeit of a different brand. As a sweetener to schools that stay in FFEL, some guaranty agencies have offered to forego the one percent "insurance premium" that they charge students (and which goes into the Federal reserve fund). At the same time, they successfully lobby Congress for an appropriations earmark (out of the mandatory account set up for direct lending). So, they are essentially using Federal money to provide a financial incentive for students and schools to stay in FFEL. Some lenders and secondary markets -- particularly Sallie Mae -- have also begun to offer deals to students, a sign that there continue to be excess profits in the system.

While competition has improved the FFEL system for schools, the management challenge for the Federal government has remained unchanged. Lenders and secondary markets are protected against default risks and interest rate risks, so assuring due diligence in collection requires detailed regulations and extensive back-end monitoring. State-based guaranty agencies were originally created to do the monitoring **and to share the risk**. But when only a few states made the financial commitment, Congress in 1976 passed laws to require the Federal government to assume virtually all of the guaranty costs, but still required a network of guaranty agencies to help administer the program. That structure, combined with a Congressionally-set payment system that bears no relation to actual costs,[1] led GAO (1993) to conclude that the Education Department "lacks sufficient leverage over guaranty agencies to achieve effective financial management and adequate program control." The agencies' connections to governors and key decision makers in Congress have made it difficult to change that structure.

There will be two opportunities to propose changes to the student loan programs in the coming Congress. Proposals with budget implications can be part of a FY 1998 Budget reconciliation bill. Second, Congress will reauthorize the Higher Education Act during 1997/98, opening up broader student aid issues, including loans. The Education Department plans to submit a proposal for reauthorization in April. The Chairman of the House authorizing committee has asked for all input by January, and plans to finish by summer 1997. This time line is probably an attempt to ensure that he has his say in the reconciliation process. The Senate will be much slower.

DISCUSSION:

Option 1 (1997 Budget) imposes various fees and reduces subsidies to lenders, guaranty agencies, and secondary markets. Other than taking back a portion of the reserve funds, it does not change the basic structure of FFEL, nor does it address the problem of differential fees in the direct versus guarantee system. The five-year savings total $3 billion, which is currently built in to the FY 1998 preliminary budget strategy.

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[1]Aggregate guaranty agency revenues (totaling an estimated $800 million in FY 1997) are derived from borrower insurance premiums, Federal administrative cost allowances (based on .85% of new loan volume), investment income from Federal reserves (an estimated $1.8 billion at the end of FY 1995), a 27% bounty on collections on defaulted loans, and payments for pre-claims assistance.

The Education Department (Option 2) proposes the maximum reductions in subsidies to lenders, secondary markets, and guaranty agencies that they believe are possible in the FFEL program, including a restructuring of guaranty agencies that requires the return of almost all Federal reserve funds held by these agencies. ED's proposal probably imposes more costs on lenders than the system can absorb without risking access problems (see description of option 2). ED proposes to use these savings to offset reductions in borrower fees in the direct and guaranteed programs in order to reduce the debt burden on borrowers, and improve the competitive position of direct lending. The five-year savings would total $2.4 billion, $600 million less than now assumed in the FY 1998 Budget strategy.

ED's restructuring proposal calls for guaranty agency agreements to expire periodically, and would eliminate their now-irrelevant statutory guaranty function, thereby making it possible to call back most of their liquid reserves -- over $2 billion -- which would be scored as receipts to offset other costs. The agencies would be paid based on their loan volume and the size of their portfolio -- still no relation to actual costs. There would be a new lender-paid "default prevention" fee, to move the focus to prevention instead of default collection. [The direct loan servicing contracts do not include financial incentives for default prevention, but we recommend that they do so.]

The PAD recommendation (Option 3) rejects the use of statutory formulas for paying for program administration. Instead, it would rely on performance-based Federal contracts to perform those essential functions now carried out by guaranty agencies. (GAs could compete for the contracts.) The PAD recommendation includes some reductions in fees for all borrowers in both programs, which can be offset by a new reduction in lender return proposed by ED and the call back of the reserve funds. The five-year savings would total $4.4 billion, or about $1.4 billion in new net savings to the preliminary FY 1998 budget strategy.

SCORING ISSUES: Two provisions of the Federal Credit Reform Act (FCRA) have major policy implications on the cost of this program, and savings that can be achieved by the direct loan program.

(1) Administrative funds: Under the FCRA, Federal administrative costs (including servicing) in the direct loan program are determined on an annual cash basis outside the subsidy calculation. Bank-servicing in the guarantee program is covered partly by borrower interest charges that are off-budget, and partly in the subsidy on a net present value basis. Federal administrative cost allowances to GAs are charged to the direct loan program's funding authority for student loan administrative funds on an annual cash basis. The net effect, in the first several years of the Direct Loan program, is a substantially lower subsidy rate for direct loans even if actual long-term costs in the two programs were identical. Because the Budget and authorizing committees felt that the budget rules gave direct lending an unfair advantage, the Budget Resolutions in FY 1996 and 1997 required CBO to use a baseline including

Federal administrative costs for the direct student loan program. (Whether or not the change was warranted, there is evidence that CBO did not apply it fairly).

The question of how to budget Federal administrative (particularly servicing) costs in credit programs to achieve greater cost effectiveness is under discussion in OMB as follow-up to the Review on Credit Reform.

Under current law and with current interest rates, the direct loan subsidy rate is about 9 points lower than that of the FFELP. Adding Federal administrative costs to the direct loan subsidy rate increases the rate by approximately 7 points. If, in addition, the reductions to FFELP subsidies proposed in this paper were enacted, ED projects that the subsidy rate for the two programs would be approximately the same, with direct lending possibly a little higher, depending on interest rate projections. CBO projections could be higher, or lower, for direct lending.

(2) Discount rate: A major driver of the subsidy rate in the direct loan program is the discount rate. In estimating net present values, the FCRA calls for the discount rate to be "the average interest rate on marketable Treasury securities of *similar maturity* to the direct loan or loan guarantee." For the student loan programs, OMB and CBO currently use the average of a 10-year to 20-year Treasury bond. Borrowers in both loan programs currently pay a variable interest rate. Some have argued that a variable rate loan reaches "maturity" each time it varies (every year, in the case of student loans). Indeed, Sallie Mae finances its lending primarily through short-term securities, both because borrower interest changes annually (up to a cap), and because the Federal government protects it from interest fluctuation every quarter. The assumption that the Federal cost-of-borrowing is the higher, longer-term rate considerably reduces the NPV of income from future payments on direct student loans, and reduces the NPV of cash default payments in the guarantee program. In other words, the savings associated with direct lending would be much larger -- even with servicing costs incorporated in the subsidy -- if the shorter-term discount rate were used. For example, under current interest rate assumptions, if the discount rate were the one-year Treasury note rate, program costs for the two loan programs would be $2-4 billion less over the FY 1998-2002 period, depending on whether savings were passed on to borrowers and lender yield were reduced further during the in-school period.

This issue has been the subject of intense discussion within OMB, and with Education, Treasury and CBO. There are at present strong differences of opinion. BRD believes that "it would be inconsistent with the Credit Reform Act (CRA) to use a short term interest rate to discount the loans made to students. The CRA requires OMB to use a discount rate equal to the average interest rate on marketable Treasury securities of similar maturity to the direct loan or loan guarantee for which the estimate is being made. Student loans mature in 16 years, and principal repayments are required on a fixed schedule over this 16-year period. While using a

1-year rate may be appropriate for estimating the private sector's valuation of the loans, it is not a valid method for measuring cost to the Government, which is the approach taken under the CRA."

Because of the large impact this rate makes on the cost of the direct student loan program, we recommend that these discussions on government-wide policy on this issue be resumed, including legislative change if appropriate.

DESCRIPTION OF OPTIONS:

Option 1: The President's 1997 Budget proposed savings: -$3 billion over FY 1998-2002, and -$.5 billion in FY 2002. This proposal would reduce subsidies to lenders, secondary markets, and guarantee agencies (GAs), and reduce Federal administrative expenses. It was not enacted. Proposed reductions in subsidies to lenders and secondary markets totaled $1.2 billion (adding a .07% loan holder fee, increasing the lender origination fee from .5% to .8%, reducing lender insurance from 98% to 95%, requiring all secondary markets to pay the same .3% offset fee charged to SLMA on new loan purchases for the life of the loan); reductions in payments to guaranty agencies of $.7 billion (reducing guaranty agency reinsurance and default collection retention, eliminating guaranty agency pre-claims assistance); and recall of $600 million in GA reserves.

Further, the Budget proposed a reduction in Federal administrative costs of $.5 billion over FY 1998-2002. In the Student Loan Reform Act of 1993, sec. 458 provided mandatory authority for administrative costs for FY 1994-1998. ED has projected a baseline for FY 1999-2002 consistent with funding in the statute for the earlier years, which had assumed moving to 100% direct lending, and experience has indicated that savings can be achieved allowing reductions in that baseline.

Option 2: Agency request savings: - $2.4 billion for FY 1998-2002, and $+.1 billion in 2002.

(1) Reducing borrower fees. Cost: $3.3 billion for FY 1998-2002, and $.8 billion in 2002. In the Direct Loan program, the borrower pays an origination fee of 4% of the loan amount to offset Federal costs. In the guaranteed loan program, the borrower pays an origination fee of 3%, and in addition, the guaranty agency (GA) has the option of charging the borrower an "insurance premium" of not more than 1% . ED proposes --

- to eliminate the 1% insurance premium that a guaranty agency may require all FFELP borrowers to pay. Cost: zero in FY 1998-2002, and zero in 2002.
- to reduce the origination fee for borrowers in the Direct Loan program from 4% to 3%. Cost: $.9 billion in FY1998-2002, and $.2 billion in 2002.

In light of criticism that some of the President's largest initiatives (Hope and Honors Scholarships) do not address the needs of low-income students, ED proposes to help needy students by reducing their fees even further. ED proposes --

- to eliminate the origination fee altogether for students receiving Stafford loans (which go only to students demonstrating need). Cost: $2.5 billion in FY 1998-2002, and $.6 billion in 2002.

(2) Restructuring guaranty agencies. Savings: -$1.5 billion over FY 1998-2002, and -$.2 billion in 2002. ED proposes to change the guarantor function, and achieve savings by requiring the return of $2 billion in reserve funds. The 1992 Amendments to the Higher Education Act clarified that the Federal government is the guarantor in the event of guaranty agency insolvency. ED is not prepared to replace GAs with contractors for the operation of the FFELP, but proposes that the Secretary continue to designate them, requiring their periodic recertification. Under ED's proposal GAs would retain enough reserves to pay lender claims until they are reimbursed by ED ($300 million), and to pay 6 months of operating costs ($100 million). In addition to the investment income from these remaining reserves, ED proposes to compensate GAs approximately $300 million annually through (a) an annual administrative cost allowance based on a percentage of new loans guaranteed, and (b) a per-loan "operations fee" based on total portfolio, budgeting these expenses on a present value basis as part of the subsidy rate, rather than budgeting them on a cash basis. Lenders would pay GAs a default prevention fee. ED proposes to raise the current statutory annual cap of $2 billion on the volume of loans that the Federal government can guarantee loans directly so that Federal insurance can be a viable alternative for loan access problems.

These savings do not represent a substantial increase over the savings in the FY 1997 Budget, but ED proposes a quite different way of achieving them. Savings in the new proposal (from recalling most of the GAs liquid reserves) were partially achieved in last year's budget by reducing the reinsurance of default claims paid by ED to GAs.

(3) Reducing return to lenders. Savings: -$3.8 billion over FY 1998-2002, and -$.8 in 2002. ED proposes to reduce lenders' return while the student is in school to the rate at which ED borrows from Treasury, reduce lender insurance from 98% to 90%, extend the .3% Sallie Mae fee on loans it holds to other secondary markets, increase the lender origination fee from .5% to .8%, and create a new loan holder fee. These savings resulting from reduced lender yield were part of the 1997 Budget.

After asserting that lenders and secondary markets could not absorb further reductions beyond those noted above, ED added an additional provision estimated to save $1.1 billion over FY 1998-2002, and $.3 billion in 2002. This proposal would require lenders to offer income-contingent repayment, including requiring lenders to absorb any losses associated with income-contingent repayment and loan cancellation after 25 years. Because some of these borrowers would have defaulted anyway, this would essentially throw much of the default risk onto lenders. ED uses these savings to cover much of the fee reduction for students in the Stafford program.

In addition to the income-contingent repayment provision, ED plans other changes to promote a "level-playing field" between the two programs, including providing borrowers with the ability to change plans as often as they choose, standardizing the terms and conditions of consolidated loans in both programs, and requiring that lenders in the FFELP that offer discounts offer them to all borrowers (no "creaming").

(4) Reduce Federal administrative costs. Savings: -$.5 billion over FY 1998-2002, and -$1 billion in 2002. [Same as option 1] In the Student Loan Reform Act of 1993, sec. 458 provided mandatory authority for administrative costs for FY 1994- 1998. ED has projected a baseline for FY 1999-2002 consistent with the estimates in the statute for the earlier years, which had assumed moving to 100% direct lending, and experience has indicated that savings can be achieved allowing reductions in that baseline.

Option 3: PAD alternative savings: -$4.4 billion over FY 1998-2002, and $.7 billion in 2002.

(1) Reduce borrower fees in direct lending in order to equalize student cost in both programs, but do not lower them even further. Cost: $.9 billion over FY 1998-2002 and $.2 billion in 2002. Eliminate the 1% insurance premium that guaranty agencies may, but sometimes do not, require all FFELP borrowers to pay [no cost], and reduce the origination fee for all borrowers in the Direct Loan program from 4% to 3% [cost: $.9 billion]. Students in both programs would therefore pay a 3% origination fee.

(2) Terminate GAs and award performance-based Federal contracts to accomplish the record-keeping, claims payment, default prevention and default collection functions. Savings: -$2 billion over FY 1998-2002 and -$.3 billion in 2002. This option would require recall of all reserves over 5 years -- leaving no working capital as proposed by ED. In addition, we believe that the contracting process will reduce costs below the payment to GAs proposed by ED. ED estimates that it will cost approximately $300 million per year in Federal funds to finance these GA functions under their restructuring proposal. Because of ED's inadequate data on realistic costs for these functions, it is not possible to estimate specific additional savings, but we believe they could be substantial if done under Federal performance-based contracts. The number of contractors needed would be much fewer than the 38 GAs now operating. There would be no need for working capital to provide float during the period that GAs have not been reimbursed by ED for default claims. Lenders could submit claims directly to ED. The competitive bidding process would result in lower unit costs than ED's proposal, which proposes a per-loan fee based on current GA expenditures, and continuation of the cost allowance based on a

percentage of new loan volume. Nonperforming contractors could be terminated with substantially less political controversy than a State agency or non-profit organization having a designation by the Secretary.

(3) Reduce return to lenders. Savings: -$2.8 billion over FY 1998-2002, and -$6 billion in 2002. This package would include the same savings as option 1, and in addition include the proposal to reduce the return to the lender during the in-school period, which was not part of the FY 1997 Budget package, and it does not propose requiring lenders to offer income-contingent repayment, which is unrealistic. We are investigating the feasibility of eliminating the provisions that provide a "floor" to lenders.

(4) Reduce Federal administrative costs. Savings: -$.5 billion over FY 1998-2002, and -$.1 billion in 2002. [Same as options 1 and 2]

RECOMMENDATION: Option 3. The PAD alternative addresses the two most pressing needs: (1) equalizing student benefits by adjusting fees and reducing excess profits, in the same way as proposed by the Education Department; and (2) restructuring guaranty agencies in a way that goes beyond the Education Department's current vision.

Either proposal for restructuring FFEL -- contracting for the essential functions performed by GAs, or shifting the incentive and payment structure of the current system -- will be opposed in Congress by supporters of the guaranteed loan program, both Republican and Democrat. Proposing performance-based, competitive contracts is a straightforward statement of how best to achieve effective cost control and program integrity. A more detailed review is needed of potential savings that could be realized under a contracting system, which we would carry out with ED and OFPP assistance.

It should be noted that the Education Department does not feel that the contracting process is feasible at this time and believes that current conditions, such as the growth of loan volume and introduction of direct lending, argue for continuation of a regulatory relationship with the GAs. The Department may strongly object to this approach, but it is not clear how the new structure proposed by ED differs, from a management perspective, from the current problem-plagued system.

We rejected further fee reductions for students not because they are undesirable, but because they are premature. This question should perhaps be reconsidered in the context of the unresolved issues regarding how accurately current Federal scoring represents Federal costs in both programs.

We do not believe it realistic for the Federal government to attempt to require banks and secondary markets to offer income-contingent repayment and cancellation of payments after 25 years, and to estimate substantial savings by transferring default losses associated with this change to lenders. Lenders have resisted all efforts to liberalize repayment options to borrowers across-the-board, and will have no incentive to offer this to all borrowers who request it. For income-contingent repayment, they could not have access to IRS to validate incomes and would be carrying small principal loans (*e.g.*, $1,500) for decades. The direct student loan program offers income-contingent repayment through loan "consolidation" into the direct loan program to borrowers who have a guaranteed loan.

The large remaining cost in both loan programs is program cost resulting from defaults. This issue should be revisited during the reauthorization process. It requires reconsideration of student and institutional eligibility requirements and standards as well as Federal management, including ED's targeting "gatekeeping" regulations on categories of programs and/or institutions exhibiting poor performance, which ED has been unwilling to do. Also, during reauthorization, consideration will be given to institutional performance standards as a supplement to or replacement for the default rate "kick-out" provision in identifying schools whose poor performance results in excessive Federal costs and program abuse, by making many needy students who attempt postsecondary education worse off by having assumed debt and not having bettered their economic circumstances.

Clinton Presidential Records
Digital Records Marker

Divider Title: **Student Loans**

Patricia A. Smith

12/20/96 12:40:15 PM

Record Type: Record

To: Robert M. Shireman/OMB/EOP

cc:
Subject: in-school return to lenders

There was some rationale for all this. CBO may not know what they are talking about, but at the time, they seemed to have done more thinking on this issue than the Administration.

CBO wrote in 1991 that interest on FFELs could be reduced to 91-day T-bills plus 2.25 during repayment, and 91-day T-bills plus 1.5 during the in-school period (when they assert lenders' servicing costs are only .5%).

In FY 99, at 10-20 T bond plus 1%, students will be paying and banks will be receiving, during the in-school as well as repayment periods, 5.72 + 1% = 6.72%. Under our proposal banks would get only 5.72% during the in-school period, but that is equal to slightly more than 91-day T-bill plus 1.5 (which happens to be 5.64 under current assumptions).

United States Senate
WASHINGTON, DC 20510-1302
OFFICIAL BUSINESS

Paul Simon U.S.S.

BOB SHIREMAN
OFFICE OF MANAGEMENT + BUDGET
EDUCATION DIVISION
NEW EXECUTIVE OFFICE BLDG
WASHINGTON DC
20503

Low
8236

RECEIVED

United States Senate

MEMORANDUM

KASSEBAUM — ON RESERVE AMDT.

"REAL SYMPATHY FOR WHAT YOU ARE SUGGESTING. I AM JUST A LITTLE UNCERTAIN ABOUT HOW SUCCESSFULLY WE CAN DO IT RIGHT NOW.

"... I THINK THERE IS MUCH MERIT"

395 - 4875 FAX

OMB 395 3429

United States Senate

MEMORANDUM

SIMON ON DATE OF

WORKING OUT AGREEMENT

WITH G.A.'S

↳ KASS ~~AGREES SAYS~~ LIKES IDEA

OF A YEAR TO "WORK THINGS

OUT."

KASS - Q'S ABOUT ADDRESSING

REG BEF 1 YR PER ON NEG.

United States Senate

MEMORANDUM

KASS: "I THINK THERE IS SOME INTEREST IN THIS." ~~&~~ APPREHENSION ABOUT DOE RUNNING ALL LOAN PROGS.

SIMON - DISGREES

KASS - WANTS MORE STUDY - WITHIN A YR. GET A REPORT ON IMPL. OF PRIV. GAS

United States Senate

MEMORANDUM

SIMON SUGGESTS ADOPTING AMDT W/ UNDERSTANDING THAT SENS. ~~[illegible]~~ WILL WORK OUT SOME KIND OF TIME PERIOD

COATS: "IDEA HAS SOME MERIT" "I do not know ramifications; I do not know how the #'s come out",

United States Senate

MEMORANDUM

COATS

"WILLING TO PURSUE ISSUE

W/ SIMON OR ANYONE ELSE

WOULD WELCOME TESTIMONY

FROM DOE, LENDERS, GAS

"IDEA WORTH EXPLORING"

SIMON: HOLDS CONTRACTING

OUT, BUT DESIRES VOTE

ON REC. OF RES.

United States Senate

MEMORANDUM

KASS - AGREES ABOUT ~~B~~ USE OF RES.

Pell - CONCERNED ABOUT REC. OF ALL RES.

COATS - ON LAW SET UP BY ~~A~~ DEMS — RATIO SET BY STATUTE

United States Senate

MEMORANDUM

KASS. Q's ABOUT
DETERMINING WHAT AMOUNT
OF REDUCTION IS NEC. AND
FEASIBLE

COATS: PROPOSES ADJUSTING
STATUTORY LIMITS

COATS: TALKS ABOUT REASON
FOR RESERVES: ~~BED~~ HELPED
DEAL W/ DEFAULTS

United States Senate

MEMORANDUM

in the lang. that we have

before us in the chairman's

suggestion, we require that

they use 50 % of their monies

to reimburse lenders. So this

is a requirement, actually

that is designed to make

sure that that res fund

is used for what is intended.

United States Senate

MEMORANDUM

Now if we can address it

~~this it~~ in some other way

as you sort through this

before it goes to the floor

we would be happy to

take a look at it

United States Senate

MEMORANDUM

Amdt on conflict of interest

COATS debated '92 and

+ rejected unworkable +

overreaching.

KASS INCLUDE D.L.??

COATS: INTERESTED AS LONG

AS ~~[illegible]~~ DC INCLUDED

~~SIMON~~:

"GOOD FAITH" SAID COATS

COATS + SIMON WORK OUT TO INCL. ALL PROBS.

December 9, 1996

Hey there Bobo! Enclosed are the illegible handwritten notes I promised. We are winding things down here. It is becoming very boring. Some staffers are getting worried about not having a job come January 1. Many who thought they had a good in with Durbin are not so convinced. Durbin's transition is going painfully slow.

I hope Durbin's people can let Simon staffers know soon. Some Simonites are really freaking out.

I imagine you're working 14 hour days. Welcome to OMB, eh? Well, I'm off to Iowa to get engaged (by the way, I bought a ring) and take a job coaching soccer and hopefully, working for the Stanley Foundation. I have an interview with the Stanley Foundation on January 13. If it works out great, if not, it won't be that bad. I am convinced that the soccer thing will work out regardless.

Take care and keep in touch. My new address as of December 20:

620 South Dodge Street, #6
Iowa City, IA 52240
319-354-5932

My best wishes,

Corbin L. Stone

TITLE IV--EDUCATION AND RELATED PROVISIONS

SEC. 4000. TABLE OF CONTENTS.

The table of contents for this title is as follows:

SUBTITLE A--HIGHER EDUCATION

SEC. 4001. SHORT TITLE; REFERENCES; AND GENERAL EFFECTIVE DATE.

(a) SHORT TITLE.--This subtitle may be cited as the "Student Loan Reform Act of 1995".

(b) REFERENCES.--Except as otherwise expressly provided, whenever in this subtitle an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.).

(c) GENERAL EFFECTIVE DATE.--Unless otherwise specified in this subtitle, the amendments made by this subtitle shall take effect on January 1, 1996.

SEC. 4002. PARTICIPATION OF INSTITUTIONS AND ADMINISTRATION OF LOAN PROGRAMS.

(a) LIMITATION ON PROPORTION OF LOANS MADE UNDER THE DIRECT LOAN PROGRAM.--Section 453(a) (20 U.S.C. 1087c(a)) is amended--

(1) by amending paragraph (2) to read as follows:

"(2) DETERMINATION OF NUMBER OF AGREEMENTS.--Notwithstanding any other provision of law, the Secretary may enter into agreements under subsections (a) and (b) of section 454 with institutions for participation in the direct loan program under this part, subject to the following:

"(A) For academic year 1994-1995, loans made under this part shall represent not more than 5 percent of new student loan volume for such year.

"(B) For academic year 1995-1996, loans made under this part, including Federal Direct Consolidation Loans, shall represent not more than 30 percent of the new student loan volume for such year, except that the Secretary shall not enter into such an agreement with an eligible institution that has not applied and been accepted for participation in the direct loan program under this part on or before September 30, 1995.

"(C) For academic year 1996-1997 and for each succeeding academic year, loans made under this part, including Federal Direct Consolidation Loans, shall represent not more than 10 percent of the new student loan volume for such year, except that only the 102 eligible institutions that participated in the direct loan program under this part for academic year 1994-1995 shall be eligible to participate in such program for academic year 1996-1997 and for each succeeding academic year.";

(2) by striking paragraph (3);

(3) by redesignating paragraph (4) as paragraph (3); and

(4) in the second sentence of paragraph (3) (as redesignated by paragraph (3)), by striking "on the most recent program data available" and inserting "on data from the academic year preceding the academic year for which the estimate is made".

(b) ELIMINATION OF CONSCRIPTION.--Section 453(b)(2) (20 U.S.C. 1087c(b)(2)) is amended--

(1) by striking subparagraph (B); and

(2) in subparagraph (A)--

(A) in clause (ii)--

(i) by striking "beginning"; and

(ii) by striking "clause (i); and" and inserting "subparagraph (A).";

(B) by redesignating clause (ii) (as amended by subparagraph (A)) as subparagraph (B); and

(C) by striking "(i) categorizing" and inserting "categorizing".

(c) CONTROL OF ADMINISTRATIVE EXPENSES.--Section 458 (20 U.S.C. 1087h) is amended--

(1) by amending subsection (a) to read as follows:

"(a) EXPENSES.--

"(1) IN GENERAL.--

"(A) IN GENERAL.--Except as provided in subparagraph (B), each fiscal year there shall be available to the

Secretary from funds not otherwise appropriated, funds to be obligated for subsidy costs under this part for the William D. Ford Federal Direct Loan Program. There shall also be available from funds not otherwise appropriated, funds to be obligated for indirect administrative expenses under this part and part B, not to exceed (from such funds not otherwise appropriated) $260,000,000 for fiscal year 1994, $345,000,000 for fiscal year 1995, $85,000,000 (and such sums as may be necessary for administrative cost allowances for guaranty agencies for costs accrued prior to January 1, 1996) for fiscal year 1996, and $85,000,000 for each of the fiscal years 1997 through 2002.

"(B) REDUCTION.--The amount authorized to be made available for fiscal year 1997 under subparagraph (A) shall be reduced by the amount of any unobligated unexpended funds available to carry out this subsection for any fiscal year prior to fiscal year 1996.

"(2) DIRECT AND INDIRECT ADMINISTRATIVE EXPENSES.--

"(A) DIRECT ADMINISTRATIVE EXPENSES.--

"(i) IN GENERAL.--For purposes of this subsection the term 'direct administrative expenses' means the cost under the William D. Ford Federal Direct Loan Program of-

"(I) activities related to credit extension, loan origination, loan servicing, management of contractors, and payments to contractors, other government entities, and program participants, under this part;

"(II) collection of delinquent loans under this part; and

"(III) write-off and closeout of loans under this part.

"(ii) CLARIFICATION WITH RESPECT TO CERTAIN EXPENSES.--Such term does not include the costs to the Department of personnel, training, rent, printing, or other administrative costs, associated with the activities described in subclause (I), (II), or (III) of clause (i).

"(B) INDIRECT ADMINISTRATIVE EXPENSES.--For purposes of this subsection the term 'indirect administrative expenses' means the cost of--

"(i) personnel engaged in developing program regulations, policy and administrative guidance;

"(ii) audits of institutions and contractors;

"(iii) program reviews; and

"(iv) other oversight of the program under this part or under part B.

"(3) SUBSIDY COST.--The term 'subsidy cost' means the estimated long-term cost to the Federal Government of direct administrative expenses calculated on a net present value basis."; and

(2) by striking subsection (d).

(d) DEFAULT RATE LIMITATIONS ON DIRECT LENDING.--

(1) INSTITUTIONAL ELIGIBILITY BASED ON DEFAULT RATES.--The first sentence of section 435(a)(2)(A) (20 U.S.C. 1085(a)(2)(A)) is amended by inserting "or part D" after "under this part".

(2) COHORT DEFAULT RATE.--Section 435(m)(1) (20 U.S.C. 1085(m)(1)) is amended--

(A) in subparagraph (A)--

(i) by striking "428, 428A, or 428H" and inserting "428, 428A, 428H, or part D (other than Federal Direct PLUS Loans)"; and

(ii) by striking "428C" and inserting "428C or 455(g)";

(B) in subparagraph (B)--

(i) by striking "only"; and

(ii) by inserting "and loans made under part D determined by the Secretary to be in default," after "for insurance,"; and

(C) in subparagraph (C), by striking "428C" and inserting "428C or 455(g)".

(3) DEFAULT RATES AND INCOME CONTINGENT REPAYMENT.--Section 435(m) (20 U.S.C. 1085(m)) is amended by adding at the end the following new paragraph:

"(5) DEFAULT RATE AND INCOME CONTINGENT REPAYMENT.--The Secretary shall prescribe regulations for the calculation of default rates for loans that are repaid pursuant to income contingent repayment under this part, which regulations shall be comparable to regulations for the calculation of default rates for loans that are repaid pursuant to income contingent repayment under part D.".

(4) TERMINATION OF INSTITUTIONAL PARTICIPATION.--Section 455 (20 U.S.C. 1087e) is amended by adding at the end the following new subsection:

"(l) TERMINATION OF INSTITUTIONS FOR HIGH DEFAULT RATES.--

"(1) METHODOLOGY AND CRITERIA.--The Secretary shall develop-

"(A) a methodology for the calculation of institutional default rates under the loan programs operated pursuant to this part;

"(B) criteria for the initiation of termination proceedings on the basis of such default rates; and

"(C) procedures for the conduct of such termination proceedings.

"(2) COMPARABILITY TO PART B.--In developing the methodology, criteria, and procedures required by paragraph (1), the Secretary, to the maximum extent possible, shall establish standards for the termination of institutions from participation in loan programs under this part that are comparable to the standards established for the termination of institutions from participation in the loan programs under part B. Such procedures shall include provisions for the appeal of default rate calculations based on deficiencies in the servicing of loans under this part that are comparable to the provisions for such appeals based on deficiencies in the servicing of loans under part B.

"(3) PROMULGATION.--The methodology, criteria, procedures and standards required by paragraphs (1) and (2) shall be promulgated in final form not later than 120 days after the date of enactment of this paragraph.".

(e) ELIMINATION OF TRANSITION TO DIRECT LOANS.--The Act (20 U.S.C. 1001 et seq.) is further amended--

(1) in section 422(c)(7) (20 U.S.C. 1072(c)(7))--

(A) in subparagraph (A), by striking "during the transition" and all that follows through "part D of this title"; and

(B) in subparagraph (B), by striking "section 428(c)(10)(F)(v)" and inserting "section 428(c)(9)(F)(v)";

(2) in section 422(g)(1) (20 U.S.C. 1072(g)(1))--

(A) in the first sentence, by striking "or the program authorized by part D of this title"; and

(B) in the second sentence, by striking "or the program authorized by part D of this title";

(3) in section 428(c)(8) (20 U.S.C. 1078(c)(8))--

(A) by striking subparagraph (B); and

(B) by striking "(A) If" and inserting "If";

(4) in section 428(c)(9)(F)(vii) (20 U.S.C. 1078(c)(9)(F)(vii))--

(A) by inserting "and" before "to avoid disruption"; and

(B) by striking ", and to ensure an orderly transition" and all that follows through the end of such clause and inserting a period;

(5) in section 428(c)(9)(K) (20 U.S.C. 1078(c)(9)(K)), by striking "the progress of the transition from the loan programs under this part to" and inserting "the integrity and administration of";

(6) in section 428(e)(1)(B)(ii) (20 U.S.C. 1078(e)(1)(B)(ii)), by striking "during the transition" and all that follows through "under part D of this title";

(7) in section 428(e)(3) (20 U.S.C. 1078(e)(3)), by striking "costs of transition" and inserting "indirect administrative expenses";

(8) in section 428(j)(3) (20 U.S.C. 1078(j)(3))--

(A) in the heading for paragraph (3), by striking "DURING TRANSITION TO DIRECT LENDING"; and

(B) in subparagraph (A), by striking "during the transition" and all that follows through "part D of this title";

(9) in the heading for paragraph (2) of section 453(c) (20 U.S.C. 1087c(c)), by striking "TRANSITION" and inserting "INSTITUTIONAL";

(10) in the heading for paragraph (3) of section 453(c) (20 U.S.C. 1087c(c)), by striking "AFTER TRANSITION"; and

(11) in section 456(b) (20 U.S.C. 1087f(b))--

(A) in paragraph (3), by inserting "and" after the semicolon;

(B) by striking paragraph (4);

(C) by redesignating paragraph (5) as paragraph (4);

and

(D) in paragraph (4) (as redesignated by subparagraph (C)), by striking "successful operation" and inserting "integrity and efficiency".

(f) FEES FOR ORIGINATION SERVICES.--Section 452 (20 U.S.C. 1087b) is amended--

(1) by striking subsection (b); and

(2) by redesignating subsections (c) and (d) as subsections (b) and (c), respectively.

(g) RISK SHARING.--Section 428(n) (20 U.S.C. 1078(n)) isamended by adding at the end the following new paragraph:

"(5) APPLICABILITY TO PART D LOANS.--The provisions of this subsection shall apply to institutions of higher education participating in direct lending under part D with respect to loans made under such part, and for the purposes of this paragraph, paragraph (4) shall be applied by inserting 'or part D' after 'this part'.".

(h) TECHNICAL AMENDMENT.--Section 428(b)(1)(X) (20 U.S.C. 1078(b)(1)(X)) is amended by striking "section 428(c)(10)" and inserting "section 428(c)(9)".

SEC. 4003. LOAN TERMS AND CONDITIONS.

(a) COMPARABILITY PROVISIONS.--

(1) IN GENERAL.--Paragraph (1) of section 455(a) (20 U.S.C. 1087e(a)) is amended to read as follows:

"(1) PARALLEL TERMS, CONDITIONS, ELIGIBILITY REQUIREMENTS, BENEFITS AND AMOUNTS.--Unless otherwise specified in this part, loans made to borrowers under this part shall have the same terms, conditions, deferments, forbearances, eligibility requirements, and benefits, be subject to the same administrative requirements for origination, payment and processing of applications, be available in the same amounts, be subject to the same interest rates and same amount of fees, and have the same repayment plans, as the corresponding types of loans made to borrowers under sections 428, 428B, and 428H. The Secretary shall promulgate regulations implementing this paragraph not later than 120 days after the date of enactment of the Student Loan Reform Act of 1995.".

(2) CONFORMING AMENDMENTS.--Section 428(b)(1) (20 U.S.C. 1078(b)(1)) is amended--

(A) in subparagraph (D)(ii), by inserting "(except pursuant to a graduated, income-sensitive, or income contingent repayment schedule)" after "10 years"; and

(B) in subparagraph (E)(ii), by inserting "(except pursuant to a graduated, income-sensitive, or income contingent repayment schedule)" after "10 years".

(b) ABILITY OF PART D BORROWERS TO OBTAIN FEDERAL STAFFORD CONSOLIDATION LOANS.--Section 428C(a)(4) (20 U.S.C. 1078-3(a)(4)) is amended--

(1) by redesignating subparagraphs (B), (C), and (D) as subparagraphs (C), (D), and (E), respectively; and

(2) by inserting after subparagraph (A) the following new subparagraph:

"(B) made under part D of this title;".

(c) ABILITY OF PART B BORROWERS TO OBTAIN FEDERAL DIRECT CONSOLIDATION LOANS.--Paragraph (5) of section 428C(b) (20 U.S.C. 1078-3(b)) is amended to read as follows:

"(5) DIRECT CONSOLIDATION LOANS FOR BORROWERS IN SPECIFIED CIRCUMSTANCES.--

"(A) Subject to subparagraphs (B) and (C) of section 453(a)(2), the Secretary may offer a borrower a Federal Direct Consolidation loan if such borrower is otherwise eligible for a consolidation loan pursuant to this section and such borrower is--

"(i) unable to obtain a consolidation loan from a lender with an agreement under subsection (a)(1) that holds one of such borrower's loans under this part; or

"(ii) unable to obtain a consolidation loan with income contingent repayment terms from a lender with an agreement under subsection (a)(1).

"(B) The Secretary shall establish appropriate certification procedures to verify the eligibility of borrowers for consolidation loans under this paragraph.

"(C) The Secretary shall not offer consolidation loans under this paragraph if, in the Secretary's judgment, the Department does not have the necessary origination and servicing arrangements in place for such loans, or the projected volume in such loans will be destabilizing to the availability of loans otherwise available under this part.".

(d) INCOME CONTINGENT REPAYMENT IN THE FEDERAL FAMILY EDUCATION LOAN PROGRAM.--

(1) INSURANCE PROGRAM AGREEMENTS.--Section 428(b)(1)(E)(i) (20 U.S.C. 1078(b)(1)(E)(i)) is amended by striking "or income-sensitive repayment schedule" and inserting "repayment schedule or an income-sensitive repayment schedule, and may, at the discretion of the lender, offer the borrower the option of repaying the loan in accordance with an income contingent repayment schedule,".

(2) REPAYMENT SCHEDULES.--The matter preceding clause (i) of section 428C(c)(2)(A) (20 U.S.C. 1078-3(c)(2)(A)) is amended--

(A) in the first sentence, by striking "or income-sensitive repayment schedules" and inserting "repayment schedules or income-sensitive repayment schedules, and may include, at the discretion of the lender, the establishment of income contingent repayment schedules"; and

(B) in the second sentence, by striking "income-sensitive" and inserting "graduated, income-sensitive, or income contingent".

(3) COMPARABLE TERMS AND CONDITIONS.--Section 428(m) (20 U.S.C. 1078(m)) is amended by adding at the end the following

new paragraph:

"(3) INCOME CONTINGENT REPAYMENT SCHEDULES.--For the purpose of this part, income contingent repayment schedules established pursuant to subsection (b)(1)(E)(i) and section 428C(c)(2)(A) shall have terms and conditions comparable to the terms and conditions established by the Secretary pursuant to section 455(e)(4). The Secretary shall discharge or cancel the indebtedness of borrowers that repay pursuant to income contingent repayment under this part to the same extent, and under the same circumstances, as the Secretary discharges or cancels the indebtedness of borrowers that repay pursuant to income contingent repayment under part D.".

(e) PLUS PROGRAM REDUCTIONS.--Section 428B(b) (20 U.S.C. 1078-2(b)) is amended--

(1) by striking "(b) LIMITATION BASED ON NEED.--" and inserting the following:

"(b) ANNUAL LIMITS.--

"(1) LIMITATION BASED ON NEED.--";

(2) by inserting before the last sentence thereof the following:

"(3) LIMITATION COMPUTED ON BASIS OF ACTUAL PAYMENTS.--"; and

(3) by inserting before paragraph (3) (as designated by the amendment made by paragraph (2) of this section) the following new paragraph:

"(2) DOLLAR LIMITATION.--Subject to paragraph (1), the maximum amount parents may borrow for one student in any academic year or its equivalent (as defined by regulations of the Secretary) is $15,000.".

SEC. 4004. AMENDMENTS AFFECTING GUARANTY AGENCIES.

(a) USE OF RESERVE FUNDS TO PURCHASE DEFAULTED LOANS.--Section 422 (20 U.S.C. 1072) is amended by adding at the end the following new subsection:

"(h) USE OF RESERVE FUNDS TO PURCHASE DEFAULTED LOANS.--

"(1) IN GENERAL.--Except as provided in paragraph (2), a guaranty agency shall use not less than 50 percent of such agency's reserve funds to purchase and hold defaulted loans that are guaranteed by such agency and for which a claim for insurance is filed with such agency by an eligible lender. The amount of such purchases shall be considered as reserve funds under this section and used in the calculation of the minimum reserve level under section 428(c)(9).

"(2) SPECIAL RULE.--A guaranty agency shall not be required to use its reserve funds to purchase and hold defaulted loans in accordance with paragraph (1) to the extent that--

"(A) the dollar volume of insurance claims filed with such agency does not amount to 50 percent of such agency's available reserve funds;

"(B) such use is prohibited by State law; or

"(C) such use will compromise the ability of the guaranty agency to pay program expenses.".

(b) EXTENSION OF PERIOD A GUARANTY AGENCY MUST HOLD A DEFAULTED LOAN.--

(1) EXEMPTION FOR EXTENDED HOLDING PERIOD.--The last sentence of section 428(c)(1)(A) (20 U.S.C. 1078(c)(1)(A)) is amended by striking "A guaranty agency" and inserting "Except as provided in section 428K, a guaranty agency".

(2) NEW EXTENDED HOLDING PERIOD PROGRAM.--

(A) AMENDMENT.--Part B of title IV (20 U.S.C. 1071 et seq.) is amended by inserting after section 428J the following new section:

"SEC. 428K. GUARANTOR PURCHASE OF CLAIMS WITH RESERVE FUNDS.

"(a) LOANS SUBJECT TO EXTENDED HOLDING PERIOD.--Except as provided in subsection (b), a guaranty agency shall file a claim for reimbursement with respect to losses (resulting from the default of a borrower) subject to reimbursement by the Secretary pursuant to section 428(c)(1) not less than 180 days nor more than 225 days after the guaranty agency discharges such agency's insurance obligation on a loan insured under this part. Such claim shall include losses on the unpaid principal and accrued interest of any such loan, including interest accrued from the date of such discharge to the date such agency files the claim for reimbursement from the Secretary.

"(b) LOANS EXCLUDED FROM EXTENDED HOLDING.--A guaranty agency may file a claim with respect to losses subject to reimbursement by the Secretary pursuant to section 428(c)(1) prior to 180 days after the date the guaranty agency discharges such agency's insurance obligation on a loan insured under this part, if--

"(1) such agency used 50 percent or more of such agency's reserve funds to purchase or hold loans in accordance with section 422(h);

"(2) such claim is based on an inability to locate the borrower and the guaranty agency certifies to the Secretary that-

"(A) diligent attempts were made to locate the borrower through the use of reasonable skip-tracing techniques in accordance with section 428(c)(2)(G); and

"(B) such skip-tracing attempts to locate the borrower were unsuccessful; or

"(3) the guaranty agency determines that the borrower is unlikely to possess the financial resources to begin repaying the loan prior to 180 days after default by the borrower.

"(c) GUARANTY AGENCY EFFORTS DURING EXTENDED HOLDING PERIOD.--A guaranty agency shall attempt to bring a loan described in subsection (a) into repayment status during the period prior to 225 days after the date the guaranty agency discharges its insurance obligation on such loan, so that no claim for reimbursement by the Secretary is necessary. Upon securing payments satisfactory to the guaranty agency during such period, such agency shall, if practicable, sell such loan to an eligible lender. Such loan shall not be sold to an eligible lender that the guaranty agency determines has substantially failed to exercise the due diligence required of lenders under this part.

"(d) REGULATION PROHIBITED.--The Secretary shall not promulgate regulations regarding the collection activity of a guaranty agency with respect to a loan described in subsection (a) for which reinsurance has not been paid under section 428(c)(1).".

(B) EFFECTIVE DATE.--The amendment made by this paragraph shall apply with respect to loans for which claims for insurance are filed by eligible lenders on or after January 1, 1996.

(c) ADMINISTRATIVE COST ALLOWANCE.--Section 428(f)(1) (20 U.S.C. 1078(f)(1)) is amended--

(1) in the matter preceding clause (i) of subparagraph (A), by striking "For a fiscal year prior to fiscal year 1994, the" and inserting "The"; and

(2) by amending subparagraph (B) to read as follows:

"(B)(i) The total amount of payments for any fiscal year prior to fiscal year 1994 made under this paragraph shall be equal to 1 percent of the total principal amount of the loans upon which insurance was issued under this part during such fiscal year by such guaranty agency.

"(ii) For the period beginning January 1, 1996 and ending September 30, 1996, and for each fiscal year thereafter, each guaranty agency shall receive an administrative cost allowance, payable quarterly, for such fiscal year calculated on the basis of 0.85 percent of the total principal amount of the loans upon which insurance was issued under this part during such fiscal year by such guaranty agency.

"(iii) The guaranty agency shall be deemed to have a contractual right against the United States to receive payments according to the provisions of this subparagraph. Payments shall be made promptly and without administrative delay to any guaranty agency submitting an accurate and complete application therefor under this subparagraph.

"(iv) Notwithstanding clauses (ii) and (iii)--

"(I) for each of the fiscal years 1996 through 1998, the Secretary shall pay an aggregate amount for such year of not more than $220,000,000 to all guaranty agencies receiving administrative cost allowances under this subparagraph; and

"(II) for each of the fiscal years 1999 through 2002, the Secretary shall pay an aggregate amount for such year of not more than $180,000,000 to all guaranty agencies receiving administrative cost allowances under this subparagraph.".

(d) SECRETARY'S EQUITABLE SHARE OF COLLECTIONS ON CONSOLIDATED DEFAULTED LOANS.--Section 428(c)(6)(A) (20 U.S.C. 1078(c)(6)(A)) is amended--

(1) in the matter preceding clause (i)--

(A) by inserting "or on behalf of" after "made by"; and

(B) by inserting ", including payments made to discharge loans made under this title to obtain a consolidation loan pursuant to this part or part D," after "borrower"; and

(2) in clause (ii), by inserting after "an amount equal to" the following: "--

"(I) for defaulted loans consolidated pursuant to this part or part D on or after January 1, 1996, 18.5 percent of the balance of the principal, accrued interest, and collection costs, outstanding at the time of such consolidation; or

"(II) for all other loans,".

(e) RESERVE FUND REFORMS.--

(1) STRENGTHENING AND STABILIZING GUARANTY AGENCIES.--Section 428(c) (20 U.S.C. 1078(c)) is amended--

(A) in paragraph (9)(C)(ii), by striking "80 percent" and inserting "76 percent"; and

(B) in paragraph (9)(E)--

(i) in the matter preceding clause (i), by striking "The Secretary may terminate a" and inserting "After providing a guaranty agency notice and opportunity for a hearing on the record, the Secretary may terminate such";

(ii) in clause (iv), by inserting "or" after the semicolon;

(iii) by striking clause (vi); and

(iv) in clause (v), by striking "; or" and inserting a period.

(2) ADDITIONAL AMENDMENTS.--Section 422 (20 U.S.C. 1072) is further amended--

(A) in the last sentence of subsection (a)(2), by striking "Except as provided in section 428(c)(10) (E) or (F), such" and inserting "Except as provided in subparagraph (E) or (F) of section 428(c)(9), such"; and

(B) in subsection (g), by amending paragraph (4) to read as follows:

"(4) DISPOSITION OF FUNDS RETURNED TO OR RECOVERED BY THE SECRETARY.--Any funds that are returned to or otherwise recovered by the Secretary pursuant to this subsection shall be returned to the Treasury of the United States for purposes of reducing the Federal debt and shall be deposited into the special account under section 3113(d) of title 31, United States Code.".

(f) ELIMINATION OF SUPPLEMENTAL PRECLAIMS ASSISTANCE.--

(1) AMENDMENT.--Section 428(l) (20 U.S.C. 1078(l)) is amended--

(A) by striking paragraph (2); and

(B) by striking "(1) PRECLAIMS" and all that follows through "Upon receipt" and inserting the following:

"(1) PRECLAIMS ASSISTANCE AND SUPPLEMENTAL PRECLAIMS ASSISTANCE.--Upon receipt".

(2) EFFECTIVE DATE.--The amendments made by this subsection shall apply to loans for which the first delinquency occurs on or after January 1, 1996.

(g) RESERVE RATIOS.--Section 428(c)(9)(A) (20 U.S.C. 1078(c)(9)(A)) is amended--

(1) in clause (i), by inserting "and" after the semicolon;

(2) in clause (ii), by striking "; and" and inserting a period; and

(3) by striking clause (iii).

(h) GUARANTY AGENCY REIMBURSEMENT.--

(1) IN GENERAL.--Section 428(c)(1) (20 U.S.C. 1078(c)(1)) is amended--

(A) in subparagraph (A), by striking "98 percent" and inserting "96 percent"; and

(B) in subparagraph (B)--

(i) in clause (i), by striking "88 percent" and inserting "86 percent"; and

(ii) in clause (ii), by striking "78 percent" and inserting "76 percent".

(2) EFFECTIVE DATE.--The amendments made by paragraph (1) shall apply with respect to loans for which the first disbursement is made on or after January 1, 1996.

SEC. 4005. AMENDMENTS AFFECTING FFELP LENDERS AND LOAN HOLDERS.

(a) RISK SHARING BY THE LOAN HOLDERS.--

(1) AMENDMENT.--Section 428(b)(1)(G) (20 U.S.C. 1078(b)(1)(G)) is amended by striking "not less than 98 percent" and inserting "95 percent".

(2) EFFECTIVE DATE.--The amendment made by this subsection shall apply with respect to loans for which the first disbursement is made on or after January 1, 1996.

(b) LENDERS-OF-LAST-RESORT.--Section 428(j)(2) (20 U.S.C. 1078(j)(2)) is amended--

(1) in subparagraph (A), by striking "60 days" and inserting "15 days"; and

(2) in subparagraph (B), by striking "two rejections from eligible lenders" and inserting "one rejection from an eligible lender".

(c) EXCEPTIONAL PERFORMANCE INSURANCE REDUCTION.--Section 428I(b)(1) (20 U.S.C. 1078-9(b)(1)) is amended--

(1) in the paragraph heading, by striking "100 PERCENT"; and

(2) by striking "100 percent" and inserting "95 percent (or 100 percent in the case of a lender-of-last-resort)".

(d) LOAN FEES FROM LENDERS.--

(1) AMENDMENT.--Section 438(d)(2) (20 U.S.C. 1087-1(d)(2))

is amended by striking "0.50 percent" and inserting "0.80 percent".

(2) EFFECTIVE DATE.--The amendment made by this subsection shall apply with respect to loans for which the first disbursement is made on or after January 1, 1996.

(e) LENDER AND HOLDER REBATE.--

(1) AMENDMENT.--Section 438 (20 U.S.C. 1078) is amended by adding at the end the following new subsection:

"(g) SUBSIDY REBATE ON STAFFORD AND PLUS LOANS.--

"(1) REBATE.--Each holder of a subsidized or unsubsidized Federal Stafford Loan under this part, or a Federal PLUS loan under section 428B, shall pay to the Secretary, on June 30 and December 31 of each year, a subsidy rebate in an amount equal to 0.035 percent of the unpaid principal amount of each such loan that such holder holds during the repayment period described in section 428(b)(7), except that, notwithstanding subparagraphs (A), (B), and (C) of section 428(b)(7), such holder shall pay a subsidy rebate under this paragraph with respect to such loan during any period of authorized forbearance.

"(2) PAYMENT OF REBATE.--The subsidy rebate shall be paid, to the extent possible, by subtracting from amounts owed such holder under section 438(b) (after deducting from such amounts any amount owed by such holder under section 438(d) for the quarters ending June 30 and December 31, as appropriate) the amount of subsidy rebates owed by such holder. To the extent the amounts owed such holder under section 438(b) (after making the deduction described in the preceding sentence) are insufficient to pay in full the subsidy rebates due from such holder, such holder shall pay the insufficiency by check or wire transfer of funds, in a manner determined by the Secretary.

"(3) DEPOSIT.--The Secretary shall deposit all subsidy rebates collected under the second sentence of paragraph (2) into the insurance fund established in section 431.".

(2) EFFECTIVE DATE.--The amendment made by this subsection shall apply with respect to loans for which the first disbursement is made on or after January 1, 1996.

(f) SMALL LENDER AUDIT EXEMPTION.--Section 428(b)(1)(U)(iii) (20 U.S.C. 1078(b)(1)(U)(iii)) is amended--

(1) by inserting "in the case of any lender that originates or holds more than $5,000,000 in principal on loans made under this title in any fiscal year" before "for (I)";

(2) in subclause (I), by inserting "such" before "lender at least once";

(3) in subclause (II), by inserting "such" before "a lender that is audited"; and

(4) by striking "if the lender" and inserting "if such lender".

SEC. 4006. CONNIE LEE PRIVATIZATION.

(a) STATUS OF THE CORPORATION AND CORPORATE POWERS; OBLIGATIONS

NOT FEDERALLY GUARANTEED.--

(1) STATUS OF THE CORPORATION.--The Corporation shall not be an agency, instrumentality, or establishment of the United States Government, nor a Government corporation nor a Government controlled corporation as such terms are defined in section 103 of title 5, United States Code. No action under section 1491 of title 28, United States Code (commonly known as the Tucker Act) shall be allowable against the United States based on the actions of the Corporation.

(2) CORPORATE POWERS.--The Corporation shall be subject to the provisions of this section, and, to the extent not inconsistent with this section, to the District of Columbia Business Corporation Act (or the comparable law of another State, if applicable). The Corporation shall have the powers conferred upon a corporation by the District of Columbia Business Corporation Act (or such other applicable State law) as from time to time in effect in order to conduct its affairs as a private, for-profit corporation and to carry out its purposes and activities incidental thereto. The Corporation shall have the power to enter into contracts, to execute instruments, to incur liabilities, to provide products and services, and to do all things as are necessary or incidental to the proper management of its affairs and the efficient operation of a private, for-profit business.

(3) LIMITATION ON OWNERSHIP OF STOCK.--

(A) SECRETARY OF THE TREASURY.--The Secretary of the Treasury, in completing the sale of stock pursuant to subsection (c), may not sell or issue the stock held by the Secretary of Education to an agency, instrumentality, or establishment of the United States Government, or to a Government corporation or a Government controlled corporation as such terms are defined in section 103 of title 5, United States Code, or to a government-sponsored enterprise as such term is defined in section 622 of title 2, United States Code.

(B) STUDENT LOAN MARKETING ASSOCIATION.--The Student Loan Marketing Association shall not increase its share of the ownership of the Corporation in excess of 42 percent of the shares of stock of the Corporation outstanding on the date of enactment of this Act. The Student Loan Marketing Association shall not control the operation of the Corporation, except that the Student Loan Marketing Association may participate in the election of directors as a shareholder, and may continue to exercise its right to appoint directors under section 754 of the Higher Education Act of 1965 (20 U.S.C. 1132f-3) as long as that section is in effect.

(C) PROHIBITION.--Until such time as the Secretary of the Treasury sells the stock of the Corporation owned by the Secretary of Education pursuant to subsection (c), the Student Loan Marketing Association shall not provide financial support or guarantees to the Corporation.

(D) FINANCIAL SUPPORT OR GUARANTEES.--After the Secretary of the Treasury sells the stock of the Corporation owned by the Secretary of Education pursuant to subsection (c), the Student Loan Marketing Association may provide financial support or guarantees to the Corporation, if such support or guarantees are subject to terms and conditions that are no more advantageous to the Corporation than the terms and conditions the Student Loan Marketing Association provides to other entities, including, where applicable, other monoline financial guaranty corporations in which the Student Loan Marketing Association has no ownership interest.

(4) NO FEDERAL GUARANTEE.--

(A) OBLIGATIONS INSURED BY THE CORPORATION.--

(i) FULL FAITH AND CREDIT OF THE UNITED STATES.--No obligation that is insured, guaranteed, or otherwise backed by the Corporation shall be deemed to be an obligation that is guaranteed by the full faith and credit of the United States.

(ii) STUDENT LOAN MARKETING ASSOCIATION.--No obligation that is insured, guaranteed, or otherwise backed by the Corporation shall be deemed to be an obligation that is guaranteed by the Student Loan Marketing Association.

(iii) SPECIAL RULE.--This paragraph shall not affect the determination of whether such obligation is guaranteed for purposes of Federal income taxes.

(B) SECURITIES OFFERED BY THE CORPORATION.--No debt or equity securities of the Corporation shall be deemed to be guaranteed by the full faith and credit of the United States.

(5) DEFINITION.--The term "Corporation" as used in this section means the College Construction Loan Insurance Association as in existence on the day before the date of enactment of this Act, and to any successor corporation.

(b) RELATED PRIVATIZATION REQUIREMENTS.--

(1) NOTICE REQUIREMENTS.--

(A) IN GENERAL.--During the six-year period following the date of enactment of this Act, the Corporation shall include, in each of the Corporation's contracts for the insurance, guarantee, or reinsurance of obligations, and in each document offering debt or equity securities of the Corporation a prominent statement providing notice that--

(i) such obligations or such securities, as the case may be, are not obligations of the United States, nor are such obligations guaranteed in any way by the full faith and credit of the United States; and

(ii) the Corporation is not an instrumentality of the United States.

(B) ADDITIONAL NOTICE.--During the five-year period following the sale of stock pursuant to subsection (c)(1), in addition to the notice requirements in subparagraph (A), the Corporation shall include, in each of the contracts and documents referred to in such subparagraph, a prominent statement providing notice that the United States is not an investor in the Corporation.

(2) CORPORATE CHARTER.--The Corporation's charter shall be amended as necessary and without delay to conform to the requirements of this section.

(3) CORPORATE NAME.--The name of the Corporation, or of any direct or indirect subsidiary thereof, may not contain the term "College Construction Loan Insurance Association", or any substantially similar variation thereof.

(4) ARTICLES OF INCORPORATION.--The Corporation shall amend its articles of incorporation without delay to reflect that one of the purposes of the Corporation shall be to guarantee, insure, and reinsure bonds, leases, and other evidences of debt of educational institutions, including Historically Black Colleges and Universities and other academic institutions which are ranked in the lower investment grade category using a nationally recognized credit rating system.

(5) REQUIREMENTS UNTIL STOCK SALE.--Notwithstanding subsection (d), the requirements of sections 754 and 760 of the Higher Education Act of 1965 (20 U.S.C. 1132f-3 and 1132f-9), as such sections were in effect on the day before the date of enactment of this Act, shall continue to be effective until the day immediately following the date of closing of the purchase of the Secretary of Education's stock (or the date of closing of the final purchase, in the case of multiple transactions) pursuant to subsection (c)(1) of this Act.

(c) SALE OF FEDERALLY OWNED STOCK.--

(1) SALE OF STOCK REQUIRED.--The Secretary of the Treasury shall sell, pursuant to section 324 of title 31, United States Code, the stock of the Corporation owned by the Secretary of Education as soon as possible after the date of enactment of this Act, but not later than six months after such date.

(2) PURCHASE BY THE CORPORATION.--In the event that the Secretary of the Treasury is unable to sell the stock, or any portion thereof, at a price acceptable to the Secretary of Education and the Secretary of the Treasury, the Corporation shall purchase, within six months after the date of enactment of this Act, such stock at a price determined by the Secretary of the Treasury and acceptable to the Corporation based on the independent appraisal of one or more nationally recognized financial firms, except that such price shall not exceed the value of the Secretary of Education's stock as determined by the Congressional Budget Office in House Report 104-153, dated June 22, 1995.

(3) REIMBURSEMENT OF COSTS OF SALE.--The Secretary of the Treasury shall be reimbursed from the proceeds of the sale of the stock under this subsection for all reasonable costs related to such sale, including all reasonable expenses relating to one or more independent appraisals under this subsection.

(4) ASSISTANCE BY THE CORPORATION.--The Corporation shall provide such assistance as the Secretary of the Treasury and the Secretary of Education may require to facilitate the sale of the stock under this subsection.

(d) REPEAL OF STATUTORY RESTRICTIONS AND RELATED PROVISIONS.--Part D of title VII of the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.) is repealed.

SEC. 4007. EXTENSION OF PROGRAM DURATION.

Part B of title IV (20 U.S.C. 1071 et seq.) is amended--

(1) in section 424(a) (20 U.S.C. 1074(a)), by striking "1998" and inserting "2002";

(2) in section 428(a)(5) (20 U.S.C. 1078(a)(5))--

(A) by striking "1998" and inserting "2002"; and

(B) by striking "2002" and inserting "2006"; and

(3) in section 428C(e) (20 U.S.C. 1078-3(e)), by amending the first sentence to read as follows: "The authority to make loans under this section expires at the close of September 30, 2002.".

HR2491 Kasich (R-OH) 11/20/95 (55282 lines)
Enrolled (finally passed both houses)

To provide for reconciliation pursuant to section 105 of the concurrent resolution on the budget for fiscal year 1996.

No special typefaces used in this bill version.
Item Key: 6965

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This item has the following provisions:

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19	SEC. 1302. EXPORT ENHANCEMENT PROGRAM.	(15 lines)
20	SUBTITLE D--MISCELLANEOUS SEC. 1401. CROP INSURANCE.	(48 lines)
21	SEC. 1402. COLLECTION AND USE OF AGRICULTURAL QUARANTINE AND INSPECTION FEES.	(76 lines)
22	SEC. 1403. COMMODITY CREDIT CORPORATION INTEREST RATE.	(7 lines)
23	TITLE II--BANKING, HOUSING, AND RELATED PROVISIONS SEC. 2001. TABLE OF CONTENTS.	(34 lines)
24	TITLE II--BANKING, HOUSING, AND RELATED PROVISIONS SUBTITLE A--FINANCIAL INSTITUTIONS SEC. 2011. SPECIAL ASSESSMENT TO CAPITALIZE SAIF.	(290 lines)
25	SEC. 2012. FINANCING CORPORATION ASSESSMENTS SHARED PROPORTIONALLY BY ALL INSURED DEPOSITORY INSTITUTIONS.	(38 lines)
26	SEC. 2013. MERGER OF BIF AND SAIF.	(483 lines)
27	SEC. 2014. CREATION OF SAIF SPECIAL RESERVE.	(41 lines)
28	SEC. 2015. REFUND OF AMOUNTS IN DEPOSIT INSURANCE FUND IN EXCESS OF DESIGNATED RESERVE AMOUNT.	(43 lines)
29	SEC. 2016. ASSESSMENT RATES FOR SAIF MEMBERS MAY NOT BE LESS THAN ASSESSMENT RATES FOR BIF MEMBERS.	(18 lines)
30	SEC. 2017. ASSESSMENTS AUTHORIZED ONLY IF NEEDED TO MAINTAIN THE RESERVE RATIO OF A DEPOSIT INSURANCE FUND.	(32 lines)
31	SEC. 2018. LIMITATION ON AUTHORITY OF OVERSIGHT BOARD TO CONTINUE TO EMPLOY MORE THAN 18 OFFICERS AND EMPLOYEES.	(38 lines)
32	SEC. 2019. DEFINITIONS.	(35 lines)
33	SUBTITLE B--HOUSING SEC. 2051. ANNUAL ADJUSTMENT FACTORS FOR OPERATING COSTS ONLY; RESTRAINT ON RENT INCREASES.	(53 lines)
34	SEC. 2052. FORECLOSURE AVOIDANCE AND BORROWER ASSISTANCE.	(113 lines)
35	TITLE III--COMMUNICATIONS AND SPECTRUM ALLOCATION PROVISIONS SEC. 3001. SPECTRUM AUCTIONS.	(255 lines)
36	TITLE IV--EDUCATION AND RELATED PROVISIONS SEC. 4000. TABLE OF CONTENTS.	(26 lines)

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38	SEC. 4002. PARTICIPATION OF INSTITUTIONS AND ADMINISTRATION OF LOAN PROGRAMS.	(245 lines)
39	SEC. 4003. LOAN TERMS AND CONDITIONS.	(115 lines)
40	SEC. 4004. AMENDMENTS AFFECTING GUARANTY AGENCIES.	(210 lines)
41	SEC. 4005. AMENDMENTS AFFECTING FFELP LENDERS AND LOAN HOLDERS.	(77 lines)
42	SEC. 4006. CONNIE LEE PRIVATIZATION.	(168 lines)
43	SEC. 4007. EXTENSION OF PROGRAM DURATION.	(12 lines)
44	SUBTITLE B--PROVISIONS RELATING TO THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 SEC. 4101. WAIVER OF MINIMUM PERIOD FOR JOINT AND SURVIVOR ANNUITY EXPLANATION BEFORE ANNUITY STARTING DATE.	(16 lines)
45	TITLE V--ENERGY AND NATURAL RESOURCES PROVISIONS SUBTITLE A--NUCLEAR REGULATORY COMMISSION ANNUAL CHARGES SEC. 5001. NUCLEAR REGULATORY COMMISSION ANNUAL CHARGES.	(9 lines)
46	SUBTITLE B--DEPARTMENT OF ENERGY ASSETS CHAPTER 1--UNITED STATES ENRICHMENT CORPORATION SEC. 5201. SHORT TITLE.	(7 lines)
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48	SEC. 5203. SALE OF THE CORPORATION.	(17 lines)
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53	SEC. 5208. TRANSFER OF CONTRACTS.	(54 lines)
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57	SEC. 5212. URANIUM TRANSFERS AND SALES.	(90 lines)

58	ANNUAL MAXIMUM DELIVERIES TO END USERS	(109 lines)
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61	SEC. 5215. APPLICATION OF CERTAIN LAWS.	(32 lines)
62	SEC. 5216. AMENDMENTS TO THE ATOMIC ENERGY ACT.	(83 lines)
63	SEC. 5217. AMENDMENTS TO OTHER LAWS.	(10 lines)
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77	SEC. 5333. LEASING PROGRAM FOR LANDS WITHIN THE COASTAL PLAIN.	(72 lines)
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81	SEC. 5337. GRANT OF LEASES BY THE SECRETARY.	(39 lines)
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