# Reforming Federal Student Aid Programs:

*With a focus on the students we serve*

*July 2009*

**The Friday the 13th Group**

*An independent coalition of financial aid administrators*

## About The Friday the 13th Group –

Formed on Friday, March 13, 2009, The Friday the 13th Group was initially composed of financial aid administrators representing about 50 schools of all types from all regions -- large/small, private/public, Direct Lending/FFELP, and proprietary. Our ranks continue to grow.

We convene regularly to discuss what we can do as financial aid administrators to facilitate a thoughtful, thorough dialogue with Congress and the Administration about how best to serve our students.

We have focused our attention on two fronts. First, we initiated a process to ensure financial aid administrators, faculty and students have a way to communicate directly with Congress. Our letter (**http://congress-letter.com/letter.php**) includes signatures and personal comments from stakeholders located in all 50 States. This effort, which is on-going, shows that there is significant public support that choice and competition are needed to maintain a healthy student loan process.

Second, we are transmitting this student loan reform proposal to Congress making the case for how best to accomplish the Administration's call for a dramatic infusion of funding for need-based financial aid. We feel strongly that stakeholders should join together to help achieve this overarching goal, while also building on the following features that are essential to meeting the needs of students, families and postsecondary institutions:

- Preserve institutional choice of loan process to leverage competition, maximize service levels, and reduce student loan defaults.
- Preserve student and parent choice of lender to ensure life-of-loan servicing.
- Provide customized default prevention and financial literacy programs.
- Protect uninterrupted loan access for students and parents and avoid significant financial and administrative burdens on thousands of postsecondary institutions at a time of budgetary constraints and pressures.

Our group is strictly a grassroots initiative, led exclusively by financial aid administrators, driven by our concern for students and the unintended consequences that come from basing reform on current political pressures without sufficient consideration of what best serves the interests of all stakeholders – students, parents, schools, and taxpayers. We hope this proposal will generate a new and open conversation about how best to help students who face financial barriers in pursuit of a postsecondary education.

**Disclaimer:** *Our framework for reform of student aid programs represents the best judgment of the financial aid members of The Friday the 13th group, whose names are listed at the end of the proposal. Neither the college nor any supporting organization is responsible for the contents of this proposal nor does it represent the stated opinion of the member's college or university.*

## Executive Summary

President Obama's Fiscal Year 2010 budget proposal for higher education has begun a timely debate on the future of federal student aid programs. For nearly two decades, the federal government has operated two major student loan programs: the Federal Family Education Loan Program (FFELP) and the William D. Ford Federal Direct Loan program (Direct Loans). Competition between these two programs, driven primarily by postsecondary institutional choice of program and borrower choice of lender, has generated significant benefits and value to millions of Americans pursuing higher education. The benefits have included new uses of technology to streamline the loan process for students, innovative programs to help students make informed decisions and avoid defaults, and high levels of service responsiveness and accountability.

The President's budget proposal highlights that in the current interest rate environment, an expanded use of federal funding for student loans can be the source of considerable budget savings that can be applied to need-based financial aid. However, the Administration's proposal would also eliminate competition and choice, in favor of a solely government run Direct Loan program. Although the goal of expanding need-based grant aid is important, more than 1,700 financial aid administrators and students from across the country are making their voices heard and asking Congress to preserve choice and competition in the federal student loan programs.[i]

Indeed, financial aid officials and students from all schools types, including those that rely exclusively on the FFELP and those that rely exclusively on Direct Loans, have signed a letter that highlights the concerns with the unintended consequences associated with President Obama's budget proposal to require all postsecondary institutions to use the Direct Loan program. Fortunately, we do not have to choose between funding substantial increases in need-based financial aid and preserving the values of choice and competition that are in place today. This paper recommends a "hybrid" approach that would take advantage of the budget scoring benefits of federal funding for all federal student loans, while preserving a competitive, customer-accountable system in the origination and servicing of student loans. This approach looks beyond past ideological battles over Direct Loans vs. FFELP, and takes a pragmatic approach to what will actually work best – from the perspective of financial aid administrators who are working directly with students every day – in order to achieve the "best of both worlds."

> *"We have participated in DL and FFELP. When we left DL and returned to FFELP it was to provide our students with a choice and greater benefits. Private lenders have provided so many needed services for students, and they have provided scholarships. The individual representatives from various lenders that we have known personally are as dedicated to the needs of the students as we are."*
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> **Maria Parker, Dir. of Student Financial Services, University of Montevallo (Alabama)**

Specifically we recommend the following:

1- Capitalize on the historic opportunity to generate funding for need-based financial aid by shifting to a model of 100 percent federal funding for all federal student loans and simplify the financial aid system for students by eliminating ACG, SMART, TEACH and SEOG, and redirect those financial resources toward need-based financial aid by significantly expanding funding for the Pell Grant and Federal Work Study (FWS) programs.

2- Preserve institutional choice of loan programs to leverage competition, maximize service levels and preserve student and parent choice of lender to ensure life-of-the-loan servicing and the continuation of customized default prevention and financial literacy programs.

3- Eliminate the significant financial and administrative burden and likely subsequent confusion and processing risks associated with requiring thousands of postsecondary institutions to switch to an entirely new loan process.

Our proposed framework would also move all students and parents to one set of loan terms, adopting the current loan terms currently available in the Direct Loan program (interest rates, repayment options, loan forgiveness programs), simplifying the student loan program for students and families.

Some proponents of the Direct Loan only solution have argued that choice and competition do not matter in a system where the federal government sets the loan terms and would be providing 100 percent of the funding. As financial aid administrators dealing with the needs of students and families every day, we strongly disagree. Competition means that loan providers remain heavily focused on providing quality service and must be accountable to students and postsecondary institutions. Competition also means that loan providers have strong financial incentives to prevent loan defaults.

Some also argue that the Direct Loan solution is necessary to make Pell Grants an entitlement. However, it is important to set the record straight: mandating that all loans be Direct Loans will not make the Pell Grant program a true entitlement program. For that to occur, much deeper budget cuts -- potentially from other student aid programs -- would need to be enacted by Congress. Our view is that there has been widespread misrepresentation of this particular issue, which has had the effect of minimizing the number of financial aid administrators willing to communicate their concerns about the President's proposal. Connecting increased funding of the Pell Grant to the student loan discussion has served to distract from the basic considerations of competition and choice.

We believe that our hybrid proposal would achieve the same level of funding for need-based financial aid and maintain competition in the student loan program to ensure the long-term interests of all students are prioritized – those who rely on the student loan program and those who need additional need-based financial aid to meet the cost of college.

Our proposed framework is aligned with the Fiscal Year 2010 budget resolution that contains language that states specifically that value-added services provided by private and non-profit lenders, loan servicers and guaranty agencies should be maintained and not reduced in any manner and that changes to the student loan system "capitalize on the current infrastructure provided by private and non-profit entities."[ii]

According to the U.S. Department of Education, more than 14 million students rely on the federal student aid system, including federal student loans, Pell Grants and campus-based programs. Taken together, the FFELP and Direct Loan programs will make more than $103 billion in new and consolidation loans available in 2009. In 2010, total student loan volume is estimated to exceed $112 billion.[iii] These figures underscore how vital it is for Congress, the Administration and the financial aid community to work

**SEC. 605. SENSE OF THE CONGRESS ON COLLEGE AFFORDABILITY AND STUDENT LOAN REFORM.**
It is the Sense of the Congress that- (1) nothing in the resolution should be construed to reduce any assistance that makes college more affordable and accessible for students including but not limited to student aid programs and services provided by nonprofit State agencies and private lenders; (2) private and non-profit lenders, originators, and loan servicers help students plan for, apply to, and pay for postsecondary education and training; (3) any reform of the federal student loan programs to ensure that students have reliable and efficient access to federal loans should include some future role for the currently involved private and non-profit entities, including state non-profits with 100% FFEL lending in the State, and capitalize on the current infrastructure provided by private and non-profit entities in order both to provide employment to many Americans during this time of economic distress and to maintain valuable services that make post-secondary education more accessible and attainable for many Americans and (4) therefore, pursuant to any changes to the student loan programs, loan processing, administration, and servicing should continue to be performed, as needed, by for-profit and non-profit entities.

together to find common ground and develop bipartisan consensus around a reform proposal that best protects the immediate and long-term needs of students and their families.

## Recommendations

Since its inception in 1965 through 2008, the FFELP has successfully provided over $800 billion in loans to students and their parents utilizing private capital. An unprecedented turn in the credit markets, however, has shown that the FFELP needs to be reformed to ensure stability for students and postsecondary institutions.

We believe that the experience gained from the implementation of the *Ensuring Continued Access to Student Loans Act* (ECASLA),[iv] and its success in preserving loan access on 75 percent of the college campuses nationwide, should serve as a model in building a student loan structure that preserves institutional choice of loan programs, consumer choice of lender and life-of-loan servicing to minimize student loan defaults.

Granting private lenders access to federal funding, as under ECASLA, and transitioning the ownership of all loans to the federal government will raise billions of dollars in savings for need-based financial aid. A federal funding model with robust competition as it exists today will ensure the loan program is responsive to the needs of students and families. It is the only workable way to ensure the extensive value-added services provided by the private sector, including non-profit guaranty agencies, will continue in the form of financial literacy, default prevention programs and person-to-person programs that assist our institutions in serving the expanding needs of students and families.

***The Ensuring Continued Access to Student Loans Act of 2007* (ECASLA)**

When capital market financing became unavailable, Congress authorized the Departments of Education and Treasury to provide FFELP lenders access to federal funds for loan financing.

Under ECASLA, lenders pool the loans they have made to serve as collateral for funds from the government that they then use to make new loans. The funds provided by the government must be repaid, with interest, within a defined period of time. If lenders cannot refinance the loans they pooled together as collateral with private capital by the time the arrangement expires, they can sell or "put" the loans to the Department of Education at par value plus a $75 fee to the lender to cover origination expenses.

Because FFELP lenders pay for their access to federal funding, and because the government will benefit from the financial interest of owning the loans that are sold or "put" to the government, the ECASLA programs produce substantial savings to the government.

As financial aid administrators who have long recognized the value of FFELP, we understand the benefits of moving away from a subsidy-based model where political dynamics and constant focus on "lender subsidies" often distract policymakers and others from focusing on the fundamental merits of the FFELP. Ending the longstanding political uncertainty surrounding both of the federal student loan programs is essential, which is why we recommend building on the best features of both the FFELP and Direct Loan programs. Too often the financial aid community's attention must be diverted away from where it should be and directed to Washington, D.C. where Congress regularly makes significant changes to the Higher Education Act of 1965 outside of the regular reauthorization process. For example, the annual congressional budget process, particularly under budget reconciliation rules designed specifically to reduce the federal budget deficit, is not the appropriate way to build broad consensus around financial aid improvements and college access and affordability.

Nonetheless, since this process is most certainly moving forward, we urge Congress to take a methodical and thorough approach by holding additional hearings and fully exploring this and other proposals for reform. It is clear to us that the only way to generate an historic level of savings for need-based financial

aid is for the government to capture the revenue from ownership of all student loans, as proposed by the President. While the President has proposed to move exclusively to Direct Loans as the means of securing ownership for the government for all federal student loans, there is another way to generate federal ownership of loans. Comparable savings can also be achieved by having private sector lenders originate loans on behalf of the federal government. Under ECASLA, which is working on most of our campuses, lenders already originate loans that can be sold to the government. We recommend that the President's plan be modified to allow lenders to originate loans that must be immediately transferred to the government. At its essence, our framework builds on what works in ECASLA by using the existing infrastructure to originate and service loans in a way that continues the competition, service and efficiency that the private sector provides, while also generating the desired savings for need-based financial aid.

In fact, the Congressional Budget Office (CBO) recently estimated that new FFELP loans made in 2009, the only year where ECASLA is in effect for the full year, will result in $11 billion for the taxpayer.[v] These substantial savings were excluded from the President's FY 2010 budget because ECASLA expires on July 1, 2010.

While the savings estimated by CBO under ECASLA clearly compare favorably to the projected savings under the President's proposal, we strongly caution that such fundamental programmatic reforms that impact millions of students and thousands of postsecondary institutions should not be driven primarily by budgetary considerations.

As evidence of this fact, the President's own Office of Management and Budget (OMB) projects dramatically different savings amounts compared to CBO. The OMB projects that savings from 100 percent Direct Loans could reach $41 billion over 10 years,[vi] an amount that has already been adjusted downward from $47 billion from when the President first released his proposal in February. The same dynamic is in play at CBO. An initial analysis of the President's proposal projected that savings could reach $94 billion over 10 years if all student loan were made under Direct Loans beginning on July 1, 2010. However, a more recent estimate was released by CBO on June 16 reduced the savings estimate to $87 billion.[vii]

In addition, we concur with Mark Kantrowitz publisher of FinAid.org and FastWeb.com (an independent financial aid expert), who has concluded that the budget savings of a federal funding model for private lenders can be constructed to meet or exceed the savings generated by the President's proposal, but also warns that budget savings projections are extremely unpredictable and highly influenced by interest rate fluctuations.

> *"Creating a Monopoly over the student loan system with Direct Lending would prove to be a very poor decision. Having competition in any business generally keeps prices low and brings new products to the market place, and it also encourages innovations that help to bring down the cost of doing business. If students were forced to use Direct Lending, I fear that not only the quality of loan benefits may be affected, but also the quality of service that students receive. We need competition in the student loan industry to maintain the balance between Direct Lending & FFELP Loans."*
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> **Chrystal Woodard, Financial Aid Counselor, Louisiana Tech University (Direct Loan school)**

According to Kantrowitz, "Even slight changes in interest rates or loan volume assumptions can have a dramatic impact on the results. While I believe that both 100% DL and a permanent version of ECASLA would yield savings to the federal government, I do not have any confidence in the amount of savings or which proposal would yield greater savings. I would express caution about using any model of the savings, including mine, to determine public policy. Given the unprecedented nature of the current economic situation, it is not possible to predict future movements in interest rates or other economic factors with any accuracy. I would express caution about assuming that the current interest rate environment will persist for any particular length of time. I recommend asking OMB and CBO to

evaluate the potential savings under a variety of economic assumptions, including high, mid and low models and a variety of retrospective models. I believe this will yield results that support multiple conflicting conclusions."[viii]

Consistent with Kantrowitz' warnings, we have concerns about moving all federal loans onto the government's books and its corresponding impact on the national debt. However, by maintaining robust private sector involvement in the student loan process, options will be preserved should private capital be needed in the future.

In summary, we recommend that Congress consider a student loan structure that embraces the following ten goals:

- Produces comparable budget savings for need-based financial aid to the President's proposal by eliminating lender subsidies.
- Transfers loan ownership from lenders to the federal government.
- Retains student choice of loan originator and allows for competition.
- Allows institutions to select the originators/servicers that best meet their needs.
- Maintains ability for institutions to use the Direct Loan process exclusively or offer it as an option for students.
- Avoids a government administered monopoly where all loan origination and loan servicing decisions are made by the U.S. Department of Education.
- Permits combined servicing of federal and non-federal loans since loan defaults increase when borrowers have multiples servicers.
- Incorporates the incentives in place today to decrease loan defaults to protect students and taxpayers.
- Protects the financial literacy, default prevention programs and person-to-person programs that assist our institutions in serving the expanding needs of students and families.
- Avoids the massive transition risk of mandating all students and more than 4,000 institutions transition to a new loan program infrastructure in advance of July 1, 2010.

1. Capitalize on the historic opportunity to generate funding for need-based financial aid by shifting to a model of 100 percent federal funding for all federal student loans and simplify the financial aid system for students by eliminating ACG, SMART, TEACH and SEOG, and redirect those financial resources toward need-based financial aid by significantly expanding funding for the Pell Grant and Federal Work Study (FWS) programs.

Due to current interest rate dynamics there is an historic opportunity to generate a record level of funding for need-based financial aid. After years of debate concerning what student loan program is cheaper for the government, consideration of the President's proposal has made it clear that the costs or savings of the two student loan programs depends primarily on interest rates and the government's cost of funds compared to the costs to raise funds in the private credit markets and compensate lenders. Right now the government's cost of funds is extremely low, while the interest rates charged to students and parents are substantially higher. This means that the government is generating revenue or earning a profit between the government's low cost of funds and the interest rates charged to students and parents.

At a recent hearing convened by the House Committee on Education and Labor, the Department of Education's Deputy Under Secretary testified that the source of the projected savings under the President's plan is directly related to the significant gap between the cost to the government to raise funds and the amount charged to students.[ix] "This is the way to think about it. These are fixed rate loans to students: 6.8% fixed rate loan for 10-25 years. Our cost of funds is here. The amount we have to pay so that loans are made are here and there is a gap. When interest rates are low that is an amount that comes to us; when it is high that is an amount we pay to participants. Depending on interest rates over the next 25 years, sometimes we have more money coming in; sometimes we have less money going out," the Deputy Under Secretary testified.

> *"We (Congress, DOE, and schools) have a unique opportunity in which we can seize this moment to work collaboratively to create a new, innovative student loan system based on our shared principles of competition and accountability which serve everyone's best interest and that students/borrowers have a right to choose an educational loan provider, which could be the federal government or a private bank, and a process that incorporates both price and service components that benefit the student."*
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> **Dewey Knight, Associate Director, University of Mississippi**

According to the Pell Institute, the disparity in degree attainment reflects the fact that, despite recent gains in access, low-income and first-generation students are still less likely to go to college than their more privileged peers. Moreover, The College Board's report, *Fulfilling the Commitment: Recommendations for Reforming Federal Student Aid*, underscores what we also believe; that the Pell Grant program is the foundation of the federal student aid system. In 2006-07, the federal government distributed about $13 billion in Pell funds to 5.2 million low- and moderate-income students. Almost 60 percent of these recipients were independent students, whose parents are not required to support their college education. Among the dependent students, almost all came from families with annual incomes below $50,000 per year. Pell Grants account for about two-thirds of federal grant aid to students. Aid to veterans and military grants make up another 27 percent of these subsidies.

In addition, the report concludes that over time, the federal student grant system has been complicated by the addition of new programs related to Pell, but with somewhat different eligibility requirements. In 2006-07, about 7 percent of Pell Grant recipients began to receive Academic Competitiveness and SMART grants, which are based on academic criteria in addition to financial criteria. The report proposes eliminating supplementary grant programs with complex eligibility requirements and using the funds to increase the generosity of Pell Grants. This program consolidation will reduce confusion among students, paperwork for colleges, and the federal bureaucracy. Moreover, this change will return the focus of the core federal grant program to increasing educational opportunities for low- and moderate-income

students.[x] At the same time we renew our focus on the Pell Grant program, we should also build on the success of the Federal Work Study (FWS) program. FWS is one of the nation's first financial aid program for college students. The Economic Opportunity Act of 1964 included provisions in order to "stimulate and promote the part-time employment of students in institutions of higher education who are from low-income families and are in need of the earnings from such employment to pursue courses of study at such institutions." Over the years, some features of FWS have changed, including moving the program to the U.S. Department of Education, and placing the program under authority of the Higher Education Act of 1965. In 1992, Congress added specific language requiring that higher education institutions allocate five (5) percent of their FWS allocation for community service jobs. This was later raised to seven (7) percent in 1998. According to The College Board, in 2008-2009, the federal government spent approximately 1.8 billion on campus-based student aid programs, included Federal Supplemental Educational Opportunity Grants, Federal Work-Study, and Federal Perkins Loans. In the end, the purpose of all federal aid programs is to help students enhance their lives, obtain a degree, and develop the skills they need to enter and succeed in the work force.

Given the challenging economic conditions, more students are requesting to work on campus as jobs in the private sector have decreased. Under the Bush Administration, funding requests for FWS were disappointingly stagnant. Postsecondary institutions know their students and are focused on helping students succeed in all areas of their educational experience. FWS funds give institutions access to one of the most needed and useful programs for assisting students in learning while working on campus. An infusion of additional FWS funds would enable postsecondary institutions to target valued resources directly to students.

FWS funds provide needy students the opportunity to earn money to help pay for educational expenses. Regardless of the type of work the student is performing, the FWS program creates an atmosphere to practice communication, interpersonal skills, time management and other work place skills within an educational and flexible environment. Institutions are able to use FWS funds to do more than address the financial burdens facing students, they are also able to mentor needy students and create a pathway to a career after graduation. FWS enhances the educational experience, adds new perspectives to study skills, and helps to develop analytic and critical thinking skills. Future employers are generally impressed with students who have job experience and have worked while attending college.

**2. Preserve institutional choice of loan programs to leverage competition, maximize service levels and preserve student and parent choice of lender to ensure life-of-the-loan servicing and the continuation of customized default prevention and financial literacy programs.**

We believe Congress should focus on all three of the solid principles of the Higher Education Act of 1965 – access, affordability and choice. Consumer and institutional choice, and the resulting competition, encourages technological innovations, unmatched customer service and financial literacy programs all to the benefit of students.

Since 1993, when the Direct Loan program was first implemented, countless student benefits have resulted from the competition between the two loan programs. Without this competition, however, improvements and student-focused benefits will likely stagnate over time and the student loan programs will be less responsive to the needs of both students and colleges.

> *"Students and parents should have a choice in where they borrow money. My concern is that the "new" process will be overwhelming for our current office staff and that [it]…, will add additional burdens to financial aid administrators, student account areas, and first and foremost the folks borrowing the funds."*
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> **Ellen Foster, Director, Spring Hill College (Alabama)**

Students and schools also benefit from the life-of-the-loan servicing, customized default prevention and financial literacy programs available in the FFELP. Under the FFELP, lenders and other service providers have powerful incentives to reduce student loan defaults. Lenders are charged a financial penalty and do not earn the revenue on the student loan asset if it defaults. These types of incentives do not exist in the Direct Loan program and therefore, we are worried that with the federal government as the only lender, the potential for defaults and delinquencies will increase substantially.

> *"Students and parents need choice …. There are so many services that FFELP lenders and guarantors provide that would have to fall upon the financial aid professionals if we are forced into DL. This just adds additional burdens on the OFA staff who are already over regulated and burdened in policing so many issues already (INS, Selective Service, drug convictions etc.). Thirty years ago we had a FISL loan program run by the "feds" and they did a lousy job of servicing and collecting the loans which in turn caused high default rates."*
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> **Mary Jane Towne-Denton, Financial Aid counselor-Loan Coordinator, University of San Diego (California)**

At a time of economic uncertainty and rising unemployment, students cannot afford to have these types of supplemental services curtailed. In addition, schools could lose their federal funding if default rates rise above a certain threshold.

Linda Castillo, Director of Financial Aid, National Polytechnic College of Science in California commented in our letter to Congress: "What happened to the idea of giving students choices? Working with both programs has given me the opportunity to note the significant difference in customer servicing of these programs. Unfortunately, DL does not have additional services needed to make this a successful repayment experience. We will lose the importance of reaching out to students and making them aware of their options as well as their responsibilities. Schools need the assistance of partners in order to successfully meet the standards regarding their individual cohort default rates."

**3. Eliminate the significant financial and administrative burden and likely subsequent confusion and processing risks associated with requiring thousands of postsecondary institutions to switch to an entirely new loan process.**

We believe Congress should move carefully and seriously consider the significant administrative burden that will be required to transition more than 4,000 higher education institutions to a single loan program administered by the Department of Education.

For most institutions, awarding financial assistance to first time freshman begins soon after acceptance letters are mailed in early February. Preparation for the awarding process begins in early November as institutions need to update their web pages, support systems and infrastructure, and award letter materials.

> *"Administering the Direct Loan process at a small school with limited staff would be problematic. Much of the reconciliation and administrative tasks are handled by lenders and that would shift to the Fin Aid/Business Offices. With no budget to hire extra staff, I am worried about being able to adequately run the program. Plus, I am worried defaults will increase without the default management strategies used by FFELP lenders…."*
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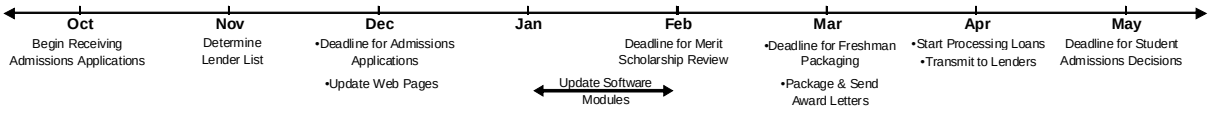
> **Martin Case, Financial Aid Director, St. Elizabeth School of Nursing (Indiana)**

It would take most institutions a minimum of eight months to one year to smoothly transition to Direct Lending. To do this, would require the redeployment of functional staff and technical staff away from their current priorities. Further, as noted by the time line below, implementation timing is critical since most institutions begin their loan process in November before the Fall semester starts.

Student aid award packages are assembled for new freshman in late February to early March before the Fall semester starts. Therefore, most institutions would need to be fully transitioned and operational in November before the Fall semester. All students need to be properly advised and will be required to complete new Master Promissory Notes. Such a massive transition will create confusion, delays, and loan access problems for students and families nationwide.

**Financial Aid Loan Processing Cycle**




According to a recent article by the *Chronicle of Higher Education*, *"Some Small Colleges Worry About the Cost of Carrying Out Obama's Loan Proposal, July 14, 2009"* if Congress adopts President Obama's student loan reform plan or a similar plan proposed by Congress, many smaller colleges and universities could be forced to spend hundreds of thousands of dollars to hire and train additional staff members and to pay for other resources such as new computer software.

The United Negro College Fund sent letters to members of Congress and officials at the Department of Education expressing concern about the administrative costs that small colleges including HBCUs could have to absorb. According

> *"University of Tampa went to direct lending for a period, but switched back to FFELP about 8 years ago. We switched back for customer service issues (for our constituents and for our counselors), our default rate went way up under direct lending, and to provide choice to our students & families."*
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> **Jackie LaTorella, Associate Director of Financial Aid, University of Tampa (Florida)**

to the article, the letters urged lawmakers to provide technical and financial support to colleges that are forced to alter their longstanding methods of processing student loans. HBCUs and other small institutions are also worried about how quickly they could transition to Direct Loan program.

Specifically, Shari Crittendon, Vice President of Government Affairs, UNCF, said: "Our concern is that smaller, private, under-resourced institutions — not just HBCU's but community colleges and small private colleges — have an additional administrative burden when switching from the federal [guaranteed-] loan program to the direct-loan program."

We believe that as the legislative process continues more institutions will be compelled, on behalf of the students they serve, to warn Congress about the risks and costs associated with mandating all schools transition to Direct Loans in a short time-frame. For example, Dewey Knight, Associate Director of Financial Aid, University of Mississippi, told *Dow Jones* (July 15) that it would take more than a year to transition. "The financial-aid process is kind of like driving the Queen Mary - it takes a whole lot of water to turn something around. The earliest a school the size of Ole Miss could implement a program switch like that proposed by the legislation would be July 1, 2011, and only if the changes were finalized this week."

In addition, Ina Sotomayor, Associate Financial Aid Director, UCLA, told the *San Francisco Chronicle* (July, 16, 2009) that switching into the Direct Loan program "would create some serious workload issues for our office at a time when resources are extremely limited. We are strong supporters of students having a choice of lenders. I'm worried about the level of support that students and schools can expect as we are going through this transition."

Moreover, we are surprised that some in Congress are moving so aggressively down a pre-determined path without gathering complete information from the very institutions that will be impacted by such a massive transition to a single loan infrastructure. One document released by the House Education and Labor Committee states the following:

> **MYTH:** ***It will cost colleges and universities already facing deep budget crises millions to switch to direct lending – leading to more tuition hikes for families.***
> This is nothing more than a myth cooked up by critics to scare colleges; there is simply no evidence to back this up. Colleges and universities that have switched to Direct Loans, including those that converted in the midst of last year's credit crisis, report that it was a fairly easy and inexpensive process, in part because schools are able use the same on-site system currently used to administer Pell Grant scholarships. Penn State, for example, did not have to hire extra staff or increase its budget during this switch last spring.[xi]

But our first-hand experience is evidence to the contrary– and we are sounding this warning voice to protect our students and our institutions. Fortunately, there are alternative options before us that do not require us to shoulder this risk. The financial aid community, the Congress and the Administration can work together to achieve an historic level of funding for need-based financial aid and serve the best interest of all stakeholders – students, parents, schools and taxpayers – by preserving the infrastructure in place on the vast majority of campuses nationwide. Again, this is aligned with the Fiscal Year 2010 budget resolution that contains language that states specifically that value-added services provided by private and non-profit lenders, loan servicers and guaranty agencies should be maintained and not reduced in any manner and that "capitalize[s] on the current infrastructure provided by private and non-profit entities."

## Conclusion

To paraphrase President Obama's remarks about health care: when it comes to student loan reform, the status quo is unsustainable. Reform is necessary. There has been much discussion about what reform would cost, and rightly so. Making thoughtful and deliberative improvements to our nation's student financial assistance programs is one of the most important steps we can take for the long-term health of America's higher education system, our country's students and our economy. We believe the experts know best: the financial aid administrators who work in the field every day and see first-hand the growing and changing needs of students and their families. We are proud to join with other key stakeholders aligning in favor, not against, reform.

The question now is, how do we finish the job and assure that the immediate and long-term needs of students, parents, schools and taxpayers are met? How do we best increase funding for need-based financial aid and still provide a reliable, quality and customer service-focused federal student loan program for students? We strongly believe that student loan reform should be guided by these simple principles: fix what's broken and build on what works. Competition, choice, customized default prevention and financial literacy programs, and responsiveness must remain top priorities. To do this, postsecondary institutions, students and parents must have a broad range of choices to ensure on-going accountability, innovation and low default rates. Specifically, we recommend that the financial aid community come together with Congress and the Administration to:

1- Capitalize on the historic opportunity to generate funding for need-based financial aid by shifting to a model of 100 percent federal funding for all federal student loans and simplify the financial aid system for students by eliminating ACG, SMART, TEACH and SEOG, and redirecting those financial resources toward need-based financial aid by significantly expanding funding for the Pell Grant and Federal Work Study (FWS) programs.

2- Preserve institutional choice of loan programs to leverage competition, maximize service levels and preserve student and parent choice of lender to ensure life-of-the-loan servicing and the continuation of customized default prevention and financial literacy programs.

3- Eliminate the significant financial and administrative burden and likely subsequent confusion and processing risks associated with requiring thousands of postsecondary institutions to switch to an entirely new loan process.

We are optimistic that this framework for reform will help facilitate collaboration between the higher education community, Congress and the Administration. We offer our expertise and experience to all policymakers and higher education stakeholder to ensure that a final reform proposal prioritizes the needs of the students we serve. Our goal is simple: we want to work cooperatively to reform the student aid programs and expand college access and affordability.

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## Letter to Congress on the Budget Resolution Proposal

The Budget Resolution Proposal would eliminate the FFEL Program effective July 1, 2010. As financial aid professionals and students, we believe this does not benefit our students and ask that you sign the following letter which will be sent to members of Congress.

April 3, 2009

Dear Senator or Delegate:

On behalf of the thousands of students that rely on federal student loans to attend college, we are writing to express our opposition to the proposed Budget Resolution and specifically the goal to eliminate the Federal Family Education Loan program (FFELP). As financial aid leaders and students representing colleges and universities from the East Coast to the West Coast, from Direct Lending and the FFEL programs, we believe the competition gained by having two programs has been a benefit to our students.

The Higher Education Act rests on three solid principles -- access, affordability, and choice. By eliminating the FFEL program, we essentially remove the ability for borrowers to choose a lender. This inherent freedom has been available for more than 40 years and with the passing of the proposed Budget Resolution, the only 'lender' available, would be the Department of Education. The Department of Education was designed to implement and ensure compliance to policy. It was not designed to be a bank. Our lending partners are experts in providing educational services to students, including life skills on budgeting and financial management, as well as ensuring repayment of loans. This public/private partnership of the FFEL program has a longstanding and proven track record which has worked successfully for millions of borrowers.

The justification for eliminating the FFEL program is to mandate Pell Grants. This certainly is needed and will provide increased opportunity to students who otherwise may not attend college. We recognize that to mandate Pell Grants within the budget, there must be a way to pay for those increased costs. The vetting through of those costs has yet to be substantiated. There are a number of expenses not considered in estimating the savings: the increase in system infrastructure needed at the Department of Education, the increase in staffing, payments to private contractors, and the cost of providing financial literacy training and management to students. Further, by having the federal government as the only lender, the potential for defaults and delinquencies to increase is substantial. Schools are held to standards regarding their individual cohort default rates and could lose their federal funding if these rates rise above a certain threshold. We should be able to continue to work with partners that aggressively promote repayment and are personally vested in the process. The calculated savings from this decision should be viewed with greater scrutiny before asking thousands of schools to make the significant infrastructure changes that will be required to properly administer a new program. Hundreds of thousands of FFEL program borrowers would need to be advised far in advance of such an entirely new program and their obligations would need to be fully explained. Rushing this legislation presents potential risk and serious public relations damage.

One other point to consider is that lenders who currently provide FFELP loans to our students also provide the funds for necessary private student loans. If those lenders are forced to leave education lending altogether, our students may not be able to borrow the private funding they need to supplement federal assistance. Even with increased Pell funding, we will still have a substantive unmet need at our schools. Many Pell recipients lack adequate resources after exhausting federal, state and institutional aid and will require additional financing options. Moreover, middle class families who do not receive Pell Grants will find themselves in need of additional student loan options after maximizing current government loan programs.

On the basis of these concerns, we urge you to oppose the administration's student loan proposal. Thank you for considering our views.

Sincerely,

## Endnotes

[i] http://congress-letter.com/letter.php

[ii] http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_reports&docid=f:hr089.pdf

[iii] http://www.whitehouse.gov/omb/budget/fy2010/assets/edu.pdf

[iv] http://federalstudentaid.ed.gov/ffelp

[v] http://www.cbo.gov/budget/factsheets/2009b/education.pdf (Table 1)

[vi] http://www.whitehouse.gov/omb/budget/fy2010/assets/trs.pdf

[vii] http://www.cbo.gov/ftpdocs/102xx/doc10296/06-16-AnalysisPresBudget_forWeb.pdf

[viii] Mark Kantrowitz: *Impact of the President's FY2010 Budget on the FFEL-DL Debate*, May 8, 2009

[ix] http://edlabor.house.gov/hearings/2009/05/increasing-student-aid-through.shtml

[x] http://professionals.collegeboard.com/profdownload/rethinking-stu-aid-fulfilling-commitment-recommendations.pdf

[xi] http://edlabor.house.gov/documents/111/pdf/publications/SAFRA-MythvFact.pdf