Republican Views

Committee Republicans are committed to maintaining the successful and robust public-private partnership that has provided low-cost and easily accessible college loans to students well for over 40 years. We have been, and remain, supportive of efforts to increase the maximum Pell Grant award and simplify the Free Application for Federal Student Aid (FAFSA). However, we believe this bill takes the wrong approach to accomplish these goals. H.R. 3221, the so-called *Student Aid and Fiscal Responsibility Act of 2009*, turns sharply in the wrong direction by eliminating the Federal Family Education Loan (FFEL) program, spending less than half of the purported "savings" on increases to Pell Grants, and raiding student aid to fund pet projects like school construction, early childhood programs, and new initiatives for community colleges.

Another Takeover by the Federal Government

Committee Republicans believe H.R. 3221 represents another attempt by President Obama and Congressional Democrats to orchestrate a federal government takeover of a private industry. The federal government has already succeeded in taking ownership of the automobile industry and controlling the actions of the financial industry. With this bill, the Department of Education, an agency intended to ensure that every child has the opportunity to learn, will now become one of the country's largest banks – originating more than $100 billion in federal student loans in the next few years.

In justifying this latest government takeover, Democrats claim the FFEL program is on "life support" and therefore must be eliminated. However, it cannot be ignored that Democrats have been trying to eliminate this program since 1993, when President Clinton put into place the Direct Loan program. What Committee Democrats refuse to acknowledge is that the FFEL program has been a stable source of private capital for more than 40 years. Private capital has temporarily dried up in the FFEL program, much like it has in the rest of the financial services sector. Yet student lending is the only sector of the financial services industry being targeted for a permanent government takeover.

Last Congress, the Committee worked in a bipartisan manner to pass H.R. 5715, the *Ensuring Continued Access to Student Loans Act* (*ECASLA*). This is one of the only economic stabilization bills that is working and is proven to save the federal government money. In fact, according to the President's fiscal year 2010 budget, this program will save the federal government $6.7 billion in fiscal year 2010 alone. Under *ECASLA*, the FFEL program successfully originated approximately $70 billion in loans and every student who needed a loan received one during the 2008-2009 academic year. Congress has passed other bills to provide liquidity to the financial marketplace or help stimulate the economy. Those bills, however, are not proving to be as successful as *ECASLA* and, in most cases have simply driven the country deeper into debt.

Committee Democrats also fail to mention that the Direct Loan program was once on "life support." In 1997, the program collapsed and was unable to make consolidation loans to borrowers. At that time, Congress did not seek to end the program. Rather, Committee

Republicans led the effort to pass emergency legislation to bail out the Direct Loan program to ensure that borrowers could receive consolidation loans.

Committee Democrats also claim the private sector is dying because most student loans being originated in the FFEL program today are being made with federal capital using the authority provided to the Secretary of Education in *ECASLA*. At the same time, Committee Democrats claim their plan will maintain the program's public-private partnership by permitting limited participation of certain private sector entities. However, both of these claims are false when the facts are examined. Despite the global credit crunch, there continues to be robust participation by the private sector under the FFEL program. There are still more than 1,500 active lenders willing to make student loans, including local lenders like the Navy Federal Credit Union, University Federal Credit Union, and Banc First, and approximately 40 percent of total FFEL loan volume is still being made using private capital.

There are also another 50 private and nonprofit loan servicers and more than 30 guaranty agencies that provide valuable services in their respective states and employ more than 30,000 private sector workers. By comparison, the U.S. Department of Education currently uses one servicer for the entire nation. While the Department recently announced that it would expand this contract to four servicers – a 400% increase from the monopoly that it was employing until recently -- this move is a poor representation of the public-private enterprise that has been effective for both students and institutions. Even the few private sector participants that are able to maintain a limited role in student lending will not be able to use the creative, personalized approaches available today. They will simply be administering a one-size-fits-all approach dictated by the federal government where market competition and effective customer service is all but eliminated.

FFEL is Better for Students and Institutions

Committee Republicans believe H.R. 3221 ignores the voices of the federal student loan consumers – the students who use the loans and the institutions that must administer the programs. Institutions have made their opinions known. When President Clinton first created the Direct Loan program in 1993, the federal government paid institutions a $10 fee for each loan, something that is classified as an "illegal inducement" under the FFEL program, and regularly pressured college presidents to join the DL program. Despite all of this pressure, the Direct Loan program only captured a total of 34 percent of loan volume at its peak in 1998. Since that time, loan volume has been around 20 percent. There has been a slight uptick in volume recently due to the global economic crisis that has affected every financial industry, including the student loan industry. However, even with the crisis and increased pressure from the Administration and Democrats in Congress, 4,400 schools, or 72 percent, remain in the FFEL program.

These schools will be forced out of FFEL under the Democrats' plan, regardless of their wishes or ability to make such a conversion. In fact, the Committee heard from institutions as recently as the day before the mark up when a group of 15 financial aid advisors released their ideas for an alternative proposal which focused on institutional choice of loan delivery system, customized default prevention and financial literacy programs, and uninterrupted loan access for students

and parents while still avoiding significant administrative and financial burdens for institutions.[1] When it comes to health care, Democrats like to promise that, "…if you like your plan, you can keep it." It's too bad they don't feel the same way about student loan programs.

The demands of students and institutions within the FFEL program have sparked fierce competition among loan providers and servicers. The competition has led to lower prices for students and institutions and innovation in loan delivery, processing, and servicing. The competition and innovation in the current FFEL program has also led to repayment incentives, interest rate reductions, fee reductions, loan forgiveness, and other financial benefits for students. Loan providers also offer broader benefits, such as college planning services, financial literacy education, default aversion, and FAFSA assistance, among other value-added services. The innovations generated by competition cannot be overlooked, even by the Department of Education, which has followed the private sector's lead and put in place many of these innovations to improve the Direct Loan program.

Committee Republicans have heard from colleges and universities that the Direct Loan program puts additional administrative burdens on schools. Switching from the FFEL program to the DL program is <u>not</u> as easy as flipping a switch. Schools must ensure that their basic software can work with the DL system. Many schools have "homegrown" software that has been specifically developed to run the schools' programs. These institutions will have to overhaul their software systems since that work will not be done by a software vendor. Institutions will also have to notify parents and students that they will have to sign new loan agreements and will have to answer questions about the new loan products. Some institutions, such as graduate schools, do not have access to the C.O.D. system that is used for loan origination, so that system will need to be added and staff will need to be trained. Finally, websites and all financial aid materials will need to be updated. This does not even take into account the number of staff from different departments that may need to stop their current tasks to help with the implementation or the projects currently underway at the institution that will have to be placed on hold to undergo the systems update necessary for the implementation of the Direct Loan program.

In talking to institutions that have been in and out of the Direct Loan program, Committee Republicans have heard that it could take anywhere between four and nine months for a large institution, with plenty of staff, to be ready to issue its first loan. In addition, we have heard that the cost to institutions of switching programs was $240,000 at one institution and $400,000 at another institution. Dr. Harris Pastides, the President of University of South Carolina, provided more specific details in a letter he sent. He stated,

> Because of the type of software developed specifically for our current computer system, our transition process is not simply a matter of purchasing and rapidly installing an 'off the shelf' program. <u>Transition to direct lending would require an investment of well over a million dollars and a timeline for implementation exceeding one year….</u>To add the cost of converting our system to direct lending without any help would be tantamount to another budget reduction for us at this time. Ironically, this would increase costs and negate much of the positive impact

[1] "Reforming Federal Student Aid Programs: Focused on the Students We Serve"

of potential increases to financial aid generated by proposed policy improvements. (Emphasis added). [2]

Gaining eligibility for the Direct Loan program and being ready to operate the program on an institution-wide basis are two very different issues that have been ignored by Congressional Democrats in their zeal to nationalize the student loan industry.

FFEL is Better for Taxpayers

Not only is the FFEL program the program of choice for students and institutions, it is good for taxpayers, too. Industry participants provide the capital up front and then share some of the risk in case the borrower defaults. Democrats may scoff that FFEL providers shoulder only three percent of the risk, but this figure represents billions of dollars that the taxpayer is not on the hook for this year. It's also a substantial amount when you realize that, under the Direct Loan program, the taxpayer is on the hook for the entire amount if a student does not repay his or her loan. The FFEL program also leverages about $70 billion in private capital each year when the financial markets are working properly. Committee Democrats want to borrow that $70 billion directly from China and our other creditors. Driving up the national debt has long-term consequences, whether it is reducing our nation's credit rating, inadvertently driving up costs, or putting us at the mercy of emerging super-powers on the other side of the globe.

Committee Democrats claim that the FFEL program simply provides profits to banks and that the Direct Loan program saves the government money. However, the facts show that the federal government has been receiving subsidies from lenders for the past several years. Since April 2006, lenders have paid $3.2 billion to the federal government. Additionally, while there are a number of factors that lead to the scoring differences between the two federal student loan programs. One undeniable factor is that a significant percentage of the "savings" in the Direct Loan program are due to the difference between the government's low cost of borrowing funds and the borrower interest rate. Committee Republicans have concerns about the federal government serving as a profit-making bank at the expense of low- and middle-income students.

Committee Democrats also claim they are making good on their promise to lower interest rates for students in H.R. 3221, but the facts show otherwise. At the beginning of the 110th Congress, Democrats rushed H.R. 5, the *College Student Relief Act*, through the House. That legislation would have reduced interest rates on student loans by half, from 6.8 percent to 3.4 percent, for all students. Immediately after the bill was introduced, Committee Democrats started to dilute their promise by scaling back interest rates from 6.8 percent to 3.4 percent over five years, but then allowing the interest rate to jump back up to 6.8 percent in 2012. At the time, *The Chronicle of Higher Education* reported that Democrats intended to make the 3.4 percent interest rate permanent in the future.[3] Additionally, *Inside Higher Ed* reported that, "Democratic staffers

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[2] Letter to The Honorable Joe Wilson, May 26, 2009.

[3] Burd, Stephen. "Democrats' Plan to Slash the Interest Rate for Student Loans Draws Criticism," The Chronicle of Higher Education, January 5, 2007. The article stated, "House Democrats briefly considered making the interest-rate cut for only one year. Then they hoped to make the cut permanent as part of legislation to renew the Higher Education Act, the law governing most federal student-aid programs, which they hope to consider later this year."

explained that budget rules and fiscal realities required that compromise. They also said that they fully expected to find money in the intervening years to make the cut permanent."[4] The bill was never considered in the Senate.

Through the budget reconciliation process that year, Democrats were able to pass H.R. 2669, the *College Cost Reduction and Access Act* -- legislation to, among other things, reduce student loan interest rates. But it was an even more diluted version of their original plan and only scaled back interest rates from 6.8 percent to 3.4 percent over four years for undergraduate students receiving subsidized loans. The legislation retained the 2012 cliff, resulting in the overall bill representing a negligible benefit for most students.

H.R. 3221 officially breaks any promises that Committee Democrats made to students when they committed to permanently lower interest rates; moreover, it ensures the federal government continues to make a profit off of the unnecessarily high level of interest being paid by students in the Direct Loan program. The bill changes the interest rate in 2012 to a variable interest rate, capped at 6.8 percent. Under this formula, it is projected that students will see an increase in their interest rates in 2012 (5.21 percent) and 2013 (6.26 percent) and will be right back up at the 6.8 percent cap in 2014.

Massive Entitlement Spending

Committee Democrats are not only forcing students to spend more under their bill, but the American taxpayers will also bear the brunt of almost $80 billion in entitlement spending at a time when the national debt is more than $11 trillion and the deficit is estimated to reach $1.8 trillion this year alone. Historically, entitlement programs such as Social Security, Medicare, Medicaid, or programs under the Child Nutrition Act were created to provide income benefits to individual citizens. Instead of recognizing this important policy, this bill spends billions of dollars in mandatory, entitlement funding on the Committee Democrats' favored political and policy causes.

While millions of families are struggling to pay their monthly bills and are thinking about which of their expenses to trim, Democrats in Congress are on a huge spending spree that will saddle our children and grandchildren with billions of debt. This bill, which Committee Democrats have portrayed as legislation to improve college access, actually contains: $6.6 billion for school construction – both at the elementary and secondary and higher education levels; $8 billion for an "early learning" initiative from birth to age 5; and $7 billion for community colleges, which may undermine our current job training system. There are major flaws with what the Democrats are proposing on school construction, early childhood education, and community colleges, but the larger issue is <u>how</u> they are pushing these proposals. Committee Democrats are putting forward a proposal to raid student aid funds and spend those entitlement dollars to bolster the funding of programs which should be within the control of the House and Senate Appropriations Committees in Congress.

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[4]Lederman, Doug. "Political Maneuvering on Student Loans," <u>Inside Higher Education</u>, January 17, 2007

Conclusion

Committee Republicans are concerned that Democrats are rushing through a risky scheme to take over the private student loan industry, regardless of the negative consequences for students and institutions. We are also very concerned that the proposed bill takes the "savings" that will result from eliminating the FFEL program and uses those funds to create a number of new programs that are not targeted toward individuals but rather toward favored political constituencies and causes. It is for these many reasons that Committee Republicans strongly oppose H.R. 3221 and urge Members of Congress to defeat this bill.

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