

Student Loan Community Proposal

Summary of Major Provisions

Summary: The Student Loan Community Proposal builds on the President's budget, combining several proposals to generate savings by financing all student loans with federal funds and allocating the full economic benefit to the federal government.

Major Provisions

Federal financing; elimination of lender subsidies: Effective July 1, 2010, all new federal student loans would be made either under a new Part K, the Competitive Federal Student Loan Program, or Part D, the Federal Direct Student Loan Program. No new loans would be made under Part B, the Federal Family Education Loan Program, and no payments would be made to lenders for interest subsidies, special allowance payments or loan defaults on the new loans.

Uniform terms and conditions: Loans made under the new Part K would have the same terms and conditions as loans made under Part D.

Choice of service provider: The Student Loan Community Proposal maintains the choice of student loan service providers that institutions of higher education currently have. Under the proposal, institutions choose the origination system that meets their school needs: either the direct loan origination system or a competitive private loan delivery system.

- ✦ Under the new program, schools would be able to choose an origination provider from loan origination providers that meet the definition of "eligible lender".
- ✦ Schools may choose two or more loan originators to serve their institution's students and families, based on their loan delivery technology, customer service, default prevention, and servicing quality and effectiveness.
- ✦ Existing code of conduct requirements are maintained.

Expanded borrower assistance and advocacy: The Student Loan Community Proposal expands borrower assistance and advocacy to all students, extending the benefits from the financial literacy and independent support services provided by today's guaranty agencies to assist students in smart borrowing choices and successful repayment, avoiding the lasting, negative consequences of default.

- ✦ Assistance provided to borrowers for all new loans originated on or after July 1, 2010.
- ✦ Assistance provided on fee-for-service basis. \$2.25 billion over the first five years, and \$5.5 billion over 10 years, is set aside for these needed services.

Existing infrastructure leveraged to ensure no transition risk and the protection of 35,000 local jobs: The Student Loan Community Proposal uses the existing student loan infrastructure for the origination, delivery, servicing, and debt management support of student loans, minimizing costs to schools and preserving tens of thousands of jobs across the country.

- ✦ The massive implementation risk under the President's plan from requiring 4,500 schools to immediately transition to the government's loan system is eliminated, thus ensuring that significant financial and administrative burdens are not passed on to schools, the supply of loan funds is not disrupted, and taxpayer savings for Pell Grants are not jeopardized.
- ✦ Loan providers would originate loans similar to today, but would immediately fund them using the federal government's low cost funds by using the programs set up under last year's successful Ensuring Continued Access to Student Loans Act (ECASLA). All of the economic benefit of the loan would accrue to the government from day one.
- ✦ Until the loan is fully disbursed, a loan would be funded in a participation agreement where the government would own 100% of the loan and receive all interest and principal payments; in return, loan providers would be paid a small amount for origination and administration:
 - Origination fee: \$20 after first participation and \$55 after full transfer;
 - Loan Administration fee: an annualized fee level of 0.69% of average principal balance of the disbursed loan.These fees are based on the fees currently set under the ECASLA. Beginning in 2012, these fees would be set through a market mechanism process managed by the Secretary of the Treasury. No origination and administration fees are paid on consolidation loans.
- ✦ Fees would be paid from administrative funds, which is how origination and servicing costs are currently funded in direct lending.
- ✦ All loans would be fully transferred to the federal government no later than 120 days after final disbursement.

Maintaining service providers to minimize borrower disruption and assure competition: The Student Loan Community Proposal combines the benefits of competitive bidding for federal servicing contracts/pricing and school-based competition. The proposal includes important enhancements to assure that schools have a broad choice of providers, including local and state-based service providers and the ability to change providers should customer service levels not meet their standards.

- ✦ Schools and students who choose to have their loans originated by servicers with servicing contracts with the Department of Education will have their loans serviced by those providers.
 - The proposal requires that the Department of Education contract with local not-for-profit and state-based servicers to expand local choice of servicing.
- ✦ Schools and students who choose to have their loans originated by providers who do not have a contract with the Department will have their loans serviced by:
 - Their loan originators if such providers are servicers and agree to service under the same terms and conditions of the Department's servicing contracts.

- A servicer of their choice from the Department servicing contracts, including the contracts for not-for-profit and state-based servicers.
- ✦ Schools that choose the direct student loan origination system can pick their servicer from those contracting with the Department of Education for direct loan servicing, including a not-for-profit or state-based servicer located in their state.

Reducing defaults by requiring “risk-sharing” for all student loan servicing. Servicers of federal student loans will reimburse the Department of Education 3% of the unpaid principal and accrued interest on any loan that defaults within the first four years of repayment, excluding periods of forbearance and deferment. By requiring “skin in the game,” servicers will go beyond prescribed compliance-driven servicing.

- ✦ “Small servicer” exclusion allows the Secretary to substitute other performance measures for risk sharing for small servicers if the Secretary determines that risk sharing combined with other terms and conditions would preclude small servicers from participating.
- ✦ “Small servicer” defined as less than \$2 billion in student loans serviced and less than \$100 million in gross revenue.
- ✦ Rates for loan servicing would reflect differences in school type.

Fee for service default collection: Default collections assigned by Department of Education based on performance of the providers of collections service, with consideration to services provided by guaranty agencies.

College Access and Completion Fund: Not-for-profit and state lenders, and guaranty agencies, would be eligible for one-third of the funding from the proposed “College Access and Completion Fund” to support financial literacy efforts, and would be eligible to compete in other initiatives sponsored by the Fund.

Extended Repayment and Graduated Repayment. Broader extended and graduated repayment terms for borrowers are reinstated, thus making better repayment terms available without the need to consolidate. These changes will help borrowers and increase taxpayer savings.

Expand ABCP conduit under ECASLA for consolidation loans. Additional taxpayer savings achieved by expanding the ABCP conduit to finance consolidation loans made between May 1, 2003, and July 1, 2009. Financing consolidation loans would provide additional financing options to resolve some outstanding liquidity issues in the student loan market while generating considerable fee income for the federal government. Consolidation loans that default while funded in the conduit would go through the regular claims process under the current student loan program.