NATIONAL DIRECT STUDENT LOAN COALITION

March 26, 2009

Dear Member of Congress:

President Obama's proposal to transfer $94 billion in lender subsidies to students merits your support. *

The President's education budget proposal includes changes to the status quo of higher education funding that will result in stabilizing and increasing Federal Pell Grant aid for needy, qualified students. Under the President's plan, Pell Grants for financially at-risk students would not only increase significantly in the short term, but also increase systematically going forward by moving Pell from discretionary to entitlement spending and indexing increases to the Consumer Price Index (CPI) plus 1%.

It is not fiscally responsible for the government to support two student loan delivery systems. However, for the past 15 years, Congress has supported both the Federal Family Education Loan Program (FFELP) and the Federal Direct Student Loan Program (DL).

- FFELP ideally (though not currently) uses private capital to loan to students, encouraged to do so by statutorily set federal subsidies, special allowance payments, and guarantees against defaults. Recently, however, it has been funded by the Treasury just like DL. There are thousands of entities who participate in FFELP loan delivery, including thousands of banks and other lenders, more than 30 guaranty agencies and numerous servicers.
- DL is a simplified system in which students at over 1600 schools receive their loans from the Department of Education, through their school, using the same process for delivering Pell, ACG, and SMART.

Today, Congress leaves the choice of loan delivery selection to the discretion of schools. However, this allows colleges and universities to decide how $94 billion in taxpayer subsidies will be spent. We are not aware of any other government program where this is allowed.

You have undoubtedly heard from FFELP industry lobbyists arguing against the President's proposal, as well as from organizations proposing hybrid loan delivery ideas that are incomplete, unproven, and inherently more expensive for taxpayers than DL. The National Direct Student Loan Coalition (NDSLC) is comprised of schools dedicated to continuous improvement and strengthening of the Direct Loan program. Our grass-roots members are financial aid professionals working at participating institutions, and we want to reassure you that the DL program is strong, proven and simple and has been working very well for students and schools for over 15 years. We have prepared the enclosed fact sheet to provide additional information about the DL program that will assist you as you deliberate this historic proposal to shift precious federal resources from lenders to students.

Please accept our best wishes and heartfelt thanks for all you do for our students, assisting them in affording the higher education they so desperately want and our country needs. You may call upon any member of the NDSLC's executive board for further information, data, or clarification.

Sincerely,

The National Direct Student Loan Coalition

**Congressional Budget Office (CBO) March 2009 estimate of the effect of President Obama's budget proposal to cancel the Federal Family Education Loan Program (FFELP) and move all student loans into the Federal Direct Student Loan Program (DL)*

Direct Loan Facts

Is choice of lender or delivery system an essential element of a successful federal student loan system?

- In no other federal financial aid program are schools or recipients provided a choice of fund delivery methods
- Loan benefits are statutorily set and virtually no FFELP lenders are providing differentiated benefits; The concept of "choice" is not relevant.

Won't a move to DL increase the national debt?

- Direct Loans are an investment that pay for themselves and even make a profit for the government. While the proceeds of Treasury auctions used for DL may be temporarily part of the national debt, the debt is paid for by the repayment of the loans. FFELP loans are considered a "contingent liability" of the federal government and, as such, are also a part of the total real debt of the government.

Can the Department of Education provide superior, consistent service in DL?

- Proven through repeated internal measurements and feedback from DL schools and borrowers, the U.S. Department of Education provides consistent and superlative service from origination of loans and borrower contact, through servicing and eventual collections. Schools continue to report their high satisfaction with contractors selected and hired by the Department to handle the DL operations. These contractors are selected based on a competitive bidding process with compensation tied to performance measures.
- Servicing in DL is handled by private sector companies, under competitive contract to the government Current FFELP servicers are now bidding on these contracts as DL expands. It is disingenuous to argue that the service would be worse, given the servicers would be the same as currently in FFELP.
- FFELP schools are reporting that they are having trouble finding lenders for their students, with many community colleges virtually red-lined by FFELP lenders.

Will default rates go up if all schools use the DL delivery system?

- The Department of Education has published the comparative default rates for DL and FFELP for each year in which the programs have operated concurrently, up to cohort year 2004. In each year except two, the DL default rate has been about 20% *lower* than in FFELP.
- In the FFELP profit model, there exists a perverse incentive in which profits are increased when borrowers default, as late fees, penalties, and collection costs are capitalized before lenders are reimbursed for the defaulted loans. Balances are so high as a result, that many borrowers can never recover.
- In the DL model, there is no profit motive driving servicers to increase borrower indebtedness. In fact, they are rewarded for keeping defaults down. Borrowers have no reason to default since Income Based Repayment and Income Contingent Repayment options can provide relief to all, regardless of their financial circumstances.

What about the loss of services that lenders and guaranty agencies provide?

- The non-statutory outreach programs currently provided by many guarantors can be worthwhile. However, the continued existence of these programs is not contingent upon FFELP's existence, and could certainly be paid for by Congress outside of the guaranty agency funding structure.
- Some FFELP lenders, guarantors, and servicers provide training to FFELP schools, as well as assistance in default management and financial literacy programming; however, their training programs are duplicative and therefore unnecessary:
  - The Department of Education provides extensive training to all schools in all areas of federal financial aid management, including DL.
  - The Department provides annual conferences, webinars, Dear Colleague Letters, etc., to educate financial aid administrators and others in legislative, regulatory, and operational issues.
  - The Department has a default management program called "Late Stage Delinquency" which has successfully assisted borrowers to prevent default. Schools are able to participate in the process or may leave the efforts to the Department.
- Schools are not and should not be dependent upon lenders and guaranty agencies for financial literacy information for their students. Many schools have mandatory financial literacy courses, and others provide superior web programs, including an exceptional course from the National Endowment for Financial Education available to all institutions at no cost.

Will the loss of FFELP mean employee layoffs?

- It is expected that current FFELP entities will participate in the competitive bidding process and become new DL contractors for the U.S. Department of Education as volume shifts from FFELP to DL. (Sallie, NelNet, and other FFELP lenders have already announced their intention to do so.) Therefore, many FFELP employees will not see job loss, just job change.
- Many of the employees engaged in FFELP activities are involved in FFELP servicing operations. Their companies have billions in outstanding student loans that will continue to need servicing and these FFELP servicers are in a position to compete for servicing contracts with the government. It is incorrect to state that all of these employees will be laid off if the President's proposal is adopted.

Has competition among FFELP lenders and between Direct Lending (DL) and FFELP really resulted in improvements to both programs?

- Undoubtedly, the competition among FFELP lenders has resulted in improvements to FFELP.
- Historically, the U.S. Department of Education has not sought to increase DL market share since its inception and as such has not competed with FFELP for market share. As a result, the Department's improvements have been instigated by their mandate to manage all federal financial aid programs to the highest standards.
- The most significant improvement to DL delivery in recent years is the implementation of the Common Origination and Delivery (COD) system, which was created as a simplified and single method for all student financial aid to be disbursed to students, including PELL, ACG, SMART, and DL.

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