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ABSTRACT

This document provides testimony, prepared statements, articles, publications, and other materials concerning the issue of augmenting current student financial assistance programs with the addition of direct student loans (Self Reliance Loans), and examines responsible ways in which the federal government should move in this direction. Among the persons providing testimony are the following: U.S. Senators Bill Bradley (New Jersey), Edward M. Kennedy (Massachusetts), Orrin G. Hatch (Utah), Nancy Landon Kassebaum (Kansas), Paul Simon (Illinois), Strom Thurmond (South Carolina), and Daniel K. Akaka (Hawaii) and U.S. Representative Thomas E. Petri (Wisconsin). Additional witnesses giving testimony or prepared statements include, among others,: John Silber, president, Boston University (Massachusetts); Father William J. Byron, president, The Catholic University, Washington, D.C.; Barry Bluestone, professor of political economy, University of Massachusetts, Boston, Massachusetts; Roxie LaFever, vice president, financial aid, University of Phoenix, Phoenix, Arizona; and Elizabeth M. Hicks, coordinator of financial aid, Harvard University, Cambridge, Massachusetts. Materials presented include "Concerns and Unanswered Questions Regarding Income Dependent Education Assistance (IDEA) aka Self Reliance Loans," and a copy of a discussion draft of a bill to amend Part D of Title IV of the Higher Education Act of 1965 to provide for income dependent education assistance. (GLR)

S. HRG. 102-515

FEDERAL DIRECT STUDENT LOANS

HEARING

BEFORE THE

COMMITTEE ON LABOR AND HUMAN RESOURCES UNITED STATES SENATE

ONE HUNDRED SECOND CONGRESS

SECOND SESSION

ON

S. 2255

TO AMEND PART D OF TITLE IV OF THE HIGHER EDUCATION ACT OF 1965 TO PROVIDE FOR INCOME DEPENDENT EDUCATION ASSISTANCE

FEBRUARY 25, 1992

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CONTENTS

STATEMENTS

TUESDAY, FEBRUARY 25, 1992

ADDITIONAL MATERIAL

FEDERAL DIRECT STUDENT LOANS

TUESDAY, FEBRUARY 25, 1992

U.S. SENATE,
COMMITTEE ON LABOR AND HUMAN RESOURCES,
Washington, DC.

The committee met, pursuant to notice, at 10:15 a.m., in room SD-430, Dirksen Senate Office Building, Senator Edward M. Kennedy (chairman of the committee) presiding.

Present: Senators Kennedy, Pell, Simon, Bingaman, Hatch, Kassebaum, Jeffords, Coats, Thurmond, Durenberger, and Cochran.

OPENING STATEMENT OF SENATOR KENNEDY

The CHAIRMAN. We'll come to order.

I first want to express appreciation to the members of our committee for their cooperation to date and to all of our witnesses who are here today on relatively short notice. We had intended to have a hearing on the issue of direct loans last Wednesday, and had given notice to the various members of the committee that was our intention. It is an issue that members of this committee have historically had great interest in and that we have considered at different times in this committee, going back to 1978, when I had the good opportunity to introduce legislation with Senator Bellmon, Senator Simon, and Congressman Buchanan, I think, were the principal cosponsors of it in the House. Senator Durenberger has been very active in this issue, Senator Bradley has as well. Senator Kassebaum, in 1978, was actually a cosponsor of the legislation. Senator Helms was a cosponsor——

Senator KASSEBAUM. Mr. Chairman, let me just say I am an older and wiser woman now. [Laughter.]

The CHAIRMAN. Well, all of us are in a constant state of developing and learning.

In any event, I did want to explain—we had set up the hearing time, and the majority leader, understanding that the Senate Finance Committee was going to be addressing the stimulus package, set the debate for the higher education bill last week, and we made some important progress toward it. We are in a situation where this issue is going to be in the House legislation—at least it has been reported out of the Education Committee in the House. The Finance Committee is addressing a proposal, and we have worked and continue to work with the members on the Finance Committee on education, health, and other issues, and we certainly will on this one.

We felt it was extremely important that those who spend a good deal of time on education issues and have special responsibilities would at least have the chance to give some consideration to those proposals. So we scheduled this hearing this morning, and I think we are very fortunate to have some people who have a very special interest in and understanding of this proposal. So we are very, very grateful to them for being here.

The idea of direct student loans from the Federal Government——

Senator HATCH. Mr. Chairman, why don't we hold off on our statements until we have listened to our colleagues, and then we can all make them. Would that be a good idea?

The CHAIRMAN. I think that's a very sensible and useful suggestion and we will do that. If there is no objection, that's the way we will proceed.

We'll ask Senator Bradley to proceed.

STATEMENT OF HON. BILL BRADLEY, A U.S. SENATOR FROM THE STATE OF NEW JERSEY

Senator BRADLEY. Thank you very much, Mr. Chairman and members of the committee, for the opportunity to appear today and speak about the issue of income-contingent direct loans.

Let me say that I believe the people of this country need another good way to help pay for college education. We have Pell Grants, we have Guaranteed Student Loans, we have SLS. I think it is important, both in terms of our long-term economic productivity and economic growth and economic theory of economic growth, recently—you have seen a whole development of the application of education ideas to growth in addition to simply labor and capital—making a compelling case for the engine of economic growth being more people going to college and being better-prepared, with more skills.

I also come at this issue because I believe that more and more Americans are becoming pessimistic about the future. In my own State of New Jersey in a poll done last summer, 52 percent of the people asked said that their children would have a lower standard of living than they do. I think an aspect of that is that the prospect of college education is drifting further and further out of their reach.

If you look at any of the numbers in the 1980's, you saw that college costs went up over 50 percent, Federal assistance went up a little over 25 percent. You saw over 600,000 kids who were eligible no longer eligible, and you saw no program that was available to nontraditional students, nontraditional students being high school kids who work for a while, women who have raised a family and want to go back to school.

It is because I think it makes economic sense in terms of higher and faster economic growth and because it makes sense in terms of restoring optimism to people's anticipation of their children's future that we augment the existing system of aid for higher education. It is with that in mind that I developed a proposal called "self-reliance scholarships," since modified by wiser minds to say "self-reliance loans."

The nub of the idea is that any American up to the age of 50 ought to be able to get up to $30,000 in order to go to college if they agree to pay a percent of their future income back into an educational trust fund until the loan is paid off, or 25 years.

That is the nub of the idea. The key is that the program be universal; it should be available to anyone. It is like an investment. And it should be income-contingent, meaning you pay a percent of your future income back into an educational trust fund.

In the original self-reliance scholarship, what I had anticipated was a menu of options where people pick, say, $10,000, and they agree to pay 2 percent of their income for 20 years into the trust fund. In the negotiations and discussions that we had surrounding this bill and responding to both Senator Durenberger and Senator Simon, and certainly the chairman and staff and people on the outside, we modified that idea to say that you should have the option of under $10,000 if you agree to pay 3, 5, or 7 percent of your income until you have paid off your loan plus the interest.

I think that this is an enormous step forward. The key point here is that it be universal, available to any American up to the age of 50, and that it be income-contingent, meaning you pay a percent of your future income back into a trust fund which, after a number of years, would be self-financing, meaning you would have available to all Americans an opportunity to finance their college education.

I want to emphasize the nontraditional aspect of this. In a changing world economy with changing demographics, the need to provide for lifetime education is enormously important. This will help 18- and 19 year-olds who want to go to college. You can obtain up to $5,000 per year from self-reliance scholarships or self-reliance loans as we have negotiated them. But it would also be available for a kid who graduates from high school, goes to work, and 10 years into work, realizes that he or she needs some more skills at the community college but has no way to finance those skill acquisitions. This would help that person to acquire those skills.

Or, take a woman who has raised a family and, at 38, wants to go back into the work force to learn and to be able to earn more. This would be available for her as well.

It would also, I think, be available for companies in a changing international marketplace that want to take advantage of community college structures to engage in retraining programs. They could in fact agree to set up a training program with a local community college and assume part of, it not all of, the repayment obligations of the individual who would receive that training.

It is flexible. I think it is important that we do this. I had hoped we could do it as part of the higher education bill. I believe that we can do it as a part of the overall budget. I think that the exact form of the bill will probably change over time, but I think that this hearing is enormously important in letting us focus on what should be the specific aspects of self-reliance loans.

I know you are concerned and interested in it. I know Senator Durenberger and Senator Simon have a deep interest in it, and I see no reason why we should not make it a part of this year's budget and action in the Finance Committee on taxes.

One final point. The reason the Finance Committee has any jurisdiction is that once you have made your agreement, once you have signed your contract, 3 percent of your income, it's like a voluntary tax, and you would have it taken out by the IRS. So that you agree to pay a voluntary tax of 3 to 5 percent of whatever your income is until you've paid back your loan plus interest. That's why the Finance Committee jurisdiction. That is also why there would be many fewer defaults—if you died, of course, there would be a default—than there are under the current system.

I hope that we are able to do it this year. I hope that we are able to get a system, another good way, not to replace Pell Grants or Guaranteed Student Loans, but another good way to help people finance their college education.

I thank the chairman very much for the opportunity to be here and for your willingness to allow me to join the committee sometime later in the morning.

The CHAIRMAN. Thank you very much. We'll look forward to your coming back.

I think that this point, other than the issue itself on the merits, is very important to understand. Unlike what our committee was considering in terms of making some adjustments in the higher education legislation, this is effectively an add-on program. It is an additional program and in no way affects the existing Pell Grants, Guaranteed Student Loan programs, or other college-based programs. I think that is important to emphasize.

We'll look forward to your coming back. I invited Senator Bradley to join the committee during the course of the morning as someone who has been a real leader in this, as well as our other colleagues who, obviously, are always welcome.

Senator Simon.

OPENING STATEMENT OF SENATOR SIMON

Senator SIMON. Thank you, Mr. Chairman.

I am pleased to join my colleagues, and I thank you for sponsoring the legislation. It has kind of come full circle. You started out sponsoring it in 1978, and we are back here now. I was pleased to learn that Senator Kassebaum was a cosponsor in 1978.

The CHAIRMAN. Senator Cochran, too.

Senator SIMON. My already high esteem for her is even higher now. [Laughter.]

Let me just remind you that the old GI bill, which we conceived of as a gift to veterans, if you put the inflation factor on would be an average of $8,100 today. And it turned out to be a huge investment in our own prosperity.

I would underscore what Bill Bradley has said. What we have to do is look at what is going to help our economy. The one term we have to be thinking about much more than we have on everything, not just this, is long-term; what is going to help this country long-term.

What you have here is something that gives help to a great many more students; it saves money for the Federal Government—and that ought to be of interest to all of us; I'm on the Budget Committee, and it certainly is there—it gives hope to families who now face major, major problems. The response from colleges and universities around the Nation has just been most heartening. They are clearly very interested.

And then, finally, we have to ask kind of a basic question. While I recognize the lending institutions are not enthusiastic for this is the Higher Education Assistance Act designed to help Sallie Mae and the lending institutions, or is it designed to help students? I think the answer ought to be very obvious.

I have some charts here, just so we can understand what it means for students. Under the present loan program—and as Bill said, we aren't replacing that; under the original proposal that Dave Durenberger and I had, you were—but you can see the present flat payback compared to an income-contingent, the slash marks there, it gradually goes up. This is on the assumption of $10,000 borrowed, $25,000 starting income, and then you put an inflation factor on. The bars are just flat. That's the present program. The one we have proposed is the next.

This is $10,000 borrowed, $16,000 annual starting income. Let's say you become a social worker. You can see what is happening on those first three payments—you end up in default, and the Federal Government picks up the tab. Under this program, you gradually pay more and more as your income goes up.

This chart shows $22,000 borrowed, $25,000 annual starting income. Again, you can see that in those first years, you are headed toward default rates unless there is a huge sacrifice. Under this program, it is phased in, the Federal Government gets its money, and you don't have the default rates.

It just seems to me, Mr. Chairman, that this is a chance to really do something for this country, to make college available to tens of thousands of additional students eventually. I recognize that at first we're just talking about 300 schools, but even there you are talking about thousands of additional students who will be able to go to college, who can get some assistance.

This is available to everyone. We don't have a means test on this. I just think it makes an awful lot of sense, and I'm pleased to be here in behalf of this program.

Thank you, Mr. Chairman.

[The prepared statement of Senator Simon (with an attachment) follows:]

Prepared Statement of Senator Simon

Mr. Chairman, thank you for the opportunity to testify this morning, and thank you for your hard work bringing all of us together on one income-contingent loan proposal.

I want to commend my colleagues Senator Bradley and Senator Durenberger for their leadership in the Finance Committee on this issue. It is fitting that this idea will be proposed as part of the economic recovery package. The most important thing we can do to improve our productivity is to invest in our human resources. Anyone who doesn't believe that student aid can help the economy should look at the old G.I. Bill. It was conceived of as a gift to veterans of World War II, nothing more. But it turned out to be a tremendous investment in our own prosperity. If you were to take that old G.I. Bill and add inflation, it would be worth today more than $8,100. And that was a grant. It is unfortunate that the Higher Education Act reauthorization bill we passed last Friday did not include a Pell Grant entitlement. But the fact that grant aid has diminished makes it that much more important that we provide students with a better loan program.

Mr. Chairman, my testimony today is really on two different subjects: (1) direct lending, and (2) income-sensitive repayment through the income tax system. While these two concepts are combined in the proposals that we all have introduced, I will address them separately.

Direct Lending

Mr. Chairman, in the current guaranteed student loan program, the Federal Government is essentially a cosigner of each loan, taking virtually full responsibility for repaying the loan if the borrower defaults. At the same time that the Federal Government takes nearly all the risk, we guarantee the lender a profit by assuring a retail rate of interest on the loan. In contrast, with direct lending the government borrows the funds at wholesale rates, saving a considerable amount of money which can be used to reduce costs to the student.

The General Accounting Office and the Congressional Budget Office agree that we could save a billion dollars, or maybe more, by shifting to a system of direct lending instead of paying subsidies to the banks, Sallie Mae, and other middle players. It would be irresponsible of us as policy-makers not to explore this option thoroughly—because if we can save money, we can use those savings to provide more aid to more students. Let me address a number of issues that have been raised about direct lending.

The Federal deficit and the Federal debt. Direct lending does not increase the Federal deficit. In fact, since we can save money that currently goes to banks and Sallie Mae, it can reduce the Federal deficit. Direct lending does increase the Federal Government's total borrowing for a number of years until the payback of loans offsets that borrowing. But the effect on the government's financial well-being is the same whether the loan is direct or guaranteed, because a guarantee is still a liability. Whether we "cosign" and subsidize the loan at a high interest rate, or make it directly at a lower interest rate, we still pay for any defaults.

Can the Education Department run a direct loan program? At the hearing on my S. 1845 last October, David Kearns made it clear that the department could run a direct loan program. I must emphasize that there is nothing revolutionary about direct assistance to students, through schools, from the Federal Government. That is how the Pell Grant program and the other campus-based programs operate; it is not a mystery. It may be legitimate to ask whether the department could oversee the collection of loans by servicers, as the House bill proposes. But our proposal uses the IRS, so this is not a problem. And the proposal that we are talking about today is only 300 schools in the first few years, so any problems can be worked out.

Can schools handle direct lending? The GAO study concluded that direct lending would simplify paperwork for schools. There is no question that schools would perform different functions under direct lending than they do under the current programs, and we do need to make sure that financial aid professionals are provided with any training or other assistance that they need. Again, by establishing a parallel program, and staring with just a few hundred schools, we can ensure a more smooth transition into the program.

How does direct lending help students? There is little disagreement about the potential of direct lending to improve service to students. In its comprehensive evaluation of guaranteed and direct lending, the National Association of Student Financial Aid Administrators (NASFAA) rated the "student service" aspects of direct lending much more favorably than the complex, error-prone guarantee system. Later witnesses can speak to this issue better than I can.

It is important to remember also that direct lending can save students money because we can pass along the savings. For example, the interest rate on IDEA/Self-Reliance is the 52-week treasury bill rate plus two percentage points, instead of an added 3.25 percentage points in the SLS program. Also, while the Senate version of the Higher Education Act reauthorization places a fee on SLS loans to make it available to more students, there is no fee on an IDEA/Self-Reliance Loan. These may sound like minor differences, but they make a huge difference to students. For example, a student who needs a total of $10,000 over four years ($2,500 a year) would leave school owing nearly $1,500 more under SLS than under IDEA, because of higher interest and fees. A student borrowing $22,000 over 5 years would owe more than $3,500 more under SLS than IDEA.

INCOME-SENSITIVE REPAYMENT

While there are benefits to direct lending alone, using the income tax system for collection has the additional advantages of providing for more efficient collection, reducing default costs, and making it possible for payments to be sensitive to the borrower's income. The many benefits of this approach are spelled out in a recent letter to higher education leaders signed by 20 college and university presidents led by Father Byron who is here today, and Myles Brand at the University of Oregon. I have attached the letter to my testimony.

Today's hearing is taking place in the midst of a national recession that, among many other things, is severely testing our present student aid structure and all of its flaws in ways that make these differences that much clearer and more dramatic. Right now, across this Nation, thousands of young adults, assaulted by the effects of the recession, are confronting the choice of making the monthly payment to the bank on a student loan, or going into default to use that money to pay the mortgage and keep the family home. And who will pick up the tab if the choice is to default? The taxpayers will.

There is a better way, a plan that would prevent this dilemma, prevent these damaged credit records, prevent these defaults, prevent the cost to the taxpayer, and give borrowers a reprieve when they need it. Income-sensitive loan repayment is that better way.

Because even if we can significantly expand grant aid—which I hope we do—there will still be a huge demand for loans, and some students will still be saddled with large debt burdens, particularly at the graduate school level. That is why we must do everything possible to ensure that money in the student loan system is not wasted on middle players and bureaucracy, and we must do what we can to minimize the negative consequences of student debt burden.

Student loan debt creates a number of problems. First, many youth and adults decide against going to college, because they are afraid they might fail, and they won't be able to pay off their loans. With an income-related program, that fear is reduced. During a period of unemployment or low wages, the required payments are reduced automatically.

Second, too many students don't do what they want to do with their lives, because of the loan payments they need to make. This might be a scientist who wants to be a high school teacher, but works for industry instead. Or a doctor who enters a high-paying specialty instead of working in an inner-city health clinic. Debt burdens skew these career decisions.

Finally, large debt burdens postpone dreams. I know a couple in Southern Illinois who are paying more than $800 a month in student loan payments. They would like to buy a home, but they simply can't afford to. Income-contingent payments would help to make their debt more manageable.

Income-sensitive payments and IRS collection also help us to address the default problem. A large part of the current problem is that people go through a low income period, default, and then never pick up where they left off. By reducing the required payment based on income, borrowers can go in and out of the system without trying to figure out who owns their loans. Also, for those people who do have money, having the IRS as the collection agency will make it much more difficult for them to avoid paying.

CONCLUSION

It is clearer today than it has ever been that we need a strategy to regain the high-wage economy our Nation once took for granted. And in any equation, education and job training must be the key elements of that strategy. A better student loan program would expand educational opportunity and invest more in our people. Opening postsecondary education to all who seek it is, in the end, not so much a gift to them as it is a gift to ourselves.

Again, I thank you for the opportunity to testify.

A CALL-TO-ACTION TO HIGHER EDUCATION LEADERS

February 1992

DEAR COLLEAGUE: A recent Washington Post poll ranking Americans' 50 greatest worries put financing higher education third. We are pleased to see national awareness of a problem all too familiar to those of us who must grapple with its consequences daily on our campuses.

We anguish over stitching together tighter and tighter budgets. We are wrestling with tuition increases, cross-subsiding more and more students, and generally struggling to keep our institutions afloat in order to keep offering the services that define our mission. We have a big problem on our hands and it is not going to be washed away by a flood of new State or Federal dollars. It demands new thinking.

One solution is to make better use of dollars we already have. We are supporting a new Federal student loan alternative that would do just that, and we urge you to join us.

This alternative approach direct student loans with universal eligibility and income-sensitive repayments has been around for a long time, but only now has it become feasible. Very simply, it is just far more efficient than current programs. Therefore, it can provide a better loan program for students and schools, while at the same time saving large amounts of money that can pay for increased grants; or for even better loan terms.

Currently, several major student loan bills are on the table in the Congress that incorporate various aspects of this approach. Their sponsors are working together toward a consensus on the issue, and any law enacted in this area is likely to have the following characteristics:

—Universal Eligibility: Loans available to all students regardless of their parents' income. The absence of any needs test greatly simplifies administration for schools, and it provides needed relief for hard-pressed middle income families.
—Direct Lending: Funds come directly from the Federal Government. Neither students nor schools need deal with banks, guarantors, or secondary markets.
—Income Dependence: Repayment is sensitive to the student's income after graduation, and operates through the income tax system—a far more effective and fair system than current collection efforts.
—Choice: Major existing programs would remain, and the new program would draw business away from them through decisions of individual schools and students that the income dependent alternative was more attractive.
—Attractive Terms: Good enough so this alternative will be a rational choice for most or many students (otherwise it will fail in the marketplace and disappear).
—Simplicity: With no needs test, no banks or guarantee agencies to deal with, and IRS collection, the program will be much simpler for everyone, including schools. Claims to the contrary, which you may have heard from people with a vested interest in current programs, are simply not true. All schools will have to do is advise students, provide lists of recipients to the Federal Government, obtain signatures on promissory notes, and provide information on repayment to borrowers.
—Huge Savings: This change could save $1 billion to $2 billion per year, depending on the details of the bill. You might ask how this is possible. The answer is that the savings come from a lower cost of capital (because of the direct lending), simpler administration, and the virtual elimination of defaults. There is neither reason to default (because payment is related to income), nor opportunity to default (because payments are income taxes). Those who would default under current programs because of low income would owe little or nothing for that year under the income dependent alternative, but would come back into repayment easily later on if their incomes rose (as most do).

In short, income dependent loans offer numerous advantages both for students and schools. All students get a convenient, affordable, and supremely flexible option that accommodates life changes and decisions such as periods of child raising, public service employment, spells of unemployment and the like. Schools can help address the growing problem of middle class student access to higher education with a program that is very simple to administer, and the savings can be used to increase grants or improve loan terms.

If we were designing student aid from scratch, we'd never come up with the current array of programs. We'd much more likely come up with something like the alternative approach just described. And now we have an unprecedented opportunity to do just that. If we miss this chance, we may not have another for a generation.

It is crucial for us to demonstrate support for this major reform. Please call or send a letter of support to your Federal Representatives and Senators. This is important. And let the major associations to which your school belongs know of your support, as well.

Thank you very much for your attention and interest.

Myles Brand, President, University of Oregon, Eugene, OR
Judith E.N. Albino, President, University of Colorado, Boulder, CO
Neil S. Bucklew, President, West Virginia University, Morgantown, WV
Leslie C. Duly, President, Bemidji State University, Bemidji, MN
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John Silber, President, Boston University, Boston, MA
James S. Walker, President, Jamestown College, Jamestown, ND

The CHAIRMAN. Thank you very much, Senator.

We'll hear from Senator Durenberger now and then come back for questions. We're delighted to have you.

OPENING STATEMENT OF SENATOR DURENBERGER

Senator DURENBERGER. Thank you, Mr. Chairman.

It was the philosopher Aristotle who said that all the great ideas are simple. What we are proposing here this morning is by no means a universal truth. The IDEA bill, the self-reliance program, are simple, simply because they provide a better way for us to help people pay for college.

The common sense rule of legislating is that "if it ain't broke, don't fix it," and there is a corollary which is some fixes make more problems than they solve. I think we are here to demonstrate again to the committee that the system is broken in many ways, that we have a new way of doing things that serves the student, the taxpayer and the Nation better.

It is truly unique because it is not a new idea; it's an older idea, as has already been indicated, whose time has finally come.

Mr. Chairman, I want to begin by thanking you for scheduling the hearing, and by saying what others have said, that you were involved in the issue long before any of us. My colleagues and I have picked up the torch more recently, and we all appreciate your leadership in giving income-contingent direct loans a chance to be tested through the legislation I hope we will adopt this year.

I also want to thank Senator Pell and my Republican colleagues who managed the higher education reauthorization bill, for their understanding of our efforts as well.

The legislation which the Senate is now considering is based on a proposal that I first introduced last summer called "IDEA," the Income-Dependent Education Act. It was originally authored in the House of Representatives by my neighbor and my mentor on this issue, Congressman Tom Petri from Wisconsin. Paul Simon and I expanded on the IDEA proposal in legislation we introduced last fall that used the savings from IDEA to help finance and expansion of the Pell Grant program. And I am pleased that the proposal the Senate is now considering also incorporates elements of similar legislation introduced by our colleague Bill Bradley.

Mr. Chairman, the IDEA proposals differ in their details, but they are all based on two simple, compelling concepts. First, college loans should be available to students directly from the Government, eliminating millions of dollars in transactional costs, administrative expenses and red tape. And second, loan payments should be based on postcollege income and be made through the IRS, eliminating millions of dollars in defaults and simplifying how loans get collected.

I asked Bob to put that second chart back up there because that represents my experience with everybody that I hire—all the college graduates who are sitting behind us in this room, and who are working in our mail rooms, working as legislative correspondents, working their way up to the prestigious seats along the wall back there. Everybody is coming in at that $16,000, $17,000, or $18,000 salary. These are the radio reporters that you meet when you go back to your local communities; people who have expensive college educations and never expected to start out by sticking a microphone in anybody's face; they really wanted to be the lawyer or the doctor or something else. And when you combine two of them as husband and wife, just take a look at that and see the problems that the current system is creating for people in the current environment.

Mr. Chairman, all across America, threatening clouds are forming over the dream of many families to send their children to college. Two months ago, a new national survey found the rising cost of college to be our third biggest worry as families in America, right behind crime and drugs, and about four worries ahead of health care.

Millions of middle-income American families are clearly worried that going to college is something that could become the sole province of the unsubsidized rich and the totally subsidized poor. And millions of American families are clearly worried that their kids won't have the same opportunities that we had just a generation ago.

What scares me the most about the trend is that it threatens to price middle-income Americans out of higher education, and as we know particularly well in this committee, that is happening at the same time that economic realities are demanding an even better-educated work force.

So unless we do something about it, we are part of a system that threatens the dreams today's students have of getting a college education.

The 21st century challenge cannot be met by our 1960's-era system of student grants and loans. And Mr. Chairman, I'll say one more time, I was involved in the beginning of this process, not at this end of it, but out at the State level where we were trying to persuade banks to get involved in this system. But it has become a system that is unnecessarily bureaucratic and complex. It is a system that largely neglects the needs of middle-income students and their families. It is a system that spends billions of dollars a year on overhead and red tape. It is a system that is vulnerable to administrative and financial problems, best documented by last year's collapse of the Higher Education Assistance Foundation. It is a system that is limiting institutional, career and family-related choices for a growing number of students, and it is a system that is burdening millions of students with inflexible loan payments and a growing level of debt that produced $3.9 billion in student loan defaults last year and $11.5 billion over the last 5 years.

What we need is a fundamentally different way both of easing the burdens of rising costs and of ensuring each of us against the uncertainties of incomes that rise and fall throughout life.

My colleagues here and I had hoped we could have taken a bigger step toward reaching that goal in this year's higher education reauthorization. I realize we still have a great deal of work to do in the Finance Committee to make the program a reality. But the legislation we are considering represents a good start on the kind of fundamental reform in the financing of higher education we need.

Before I close, Mr. Chairman, I would briefly address the concerns that have been raised about the impact a direct loan program like IDEA might have on banks, guaranty agencies and other third parties.

There are many legitimate concerns to be raised about the mechanics of income-contingent direct loans, and great care is going to be needed in crafting the details of a plan that is financially feasible to both borrowers and Government. That is why my colleague Paul Simon and I have spent a considerable amount of time with the administration, with Secretary Alexander and with the people at OMB, trying to find out what they think are some of the potential problems.

But I must state as clearly as I can, Mr. Chairman, that I don't believe the interests of third parties should be the overriding consideration in what we do. The purpose of the Federal student loan program is to help provide financial access to higher education—not offer a guaranteed source of income for banks. If students, institutions, and taxpayers can be better served by a different way of doing things, then I must say why not.

And I would remind those interested parties that the legislation we are now considering does not eliminate any existing program or the role of those who administer them. If in the future students and their colleges prefer the IDEA program, the self-reliance program, if those choices reduce demand for existing programs, then, Mr. Chairman, the marketplace has spoken.

IDEA is a far-reaching proposal because it confronts a fundamental and pervasive problem—the middle class being priced out of an essential part of the American dream. It deals with a lot of money. It deals with cutting out transactional costs. It runs up against powerful special interests. It challenges deepseated ideology, no question about it. But the system we have is broken. It costs too much, and it serves too few. And by its inflexibility, it dictates career choices that aren't necessarily what this country needs.

It will not serve the American people adequately in the 21st century. The system we have now must be changed.

In conclusion, I will just read to you the best statement I have heard on the subject which comes neither from Bradley, nor Simon, nor I. It reads as follows: "I have seen the needs of young people, needs which must be answered. I have seen the needs of their parents, needs which must be answered. And I have seen the needs of our country for a better-educated people, needs which must be answered. We believe that this particular program, Mr. President, is going to offer new opportunities for young Americans to attend college. It is going to strengthen educational opportunity for millions of Americans who today are denied that opportunity because they have been denied the financing for it. And by strengthening this opportunity, we strengthen our country. The legislation introduced today will help us achieve our objectives and will do so at the same cost as the present student loan programs. This program is good for the student, it is good for their parents, it is good for higher education, and it is financially sound."

Mr. Chairman, those are your words on July 30, 1979, introducing the bill we have already spoken of.

The CHAIRMAN. Well-stated. [Laughter.] We thank you.

I'm going to resist any questions. We have had a good opportunity to work very closely with you, and I just want to make one observation. The promise of this program is simplicity and economy. It should be cheaper. That's what we're hopeful of doing.

But as Senators Durenberger, Simon and Bradley have said, it is complicated, and the more you get into it, I think all of us have seen the challenges it presents.

I will be introducing the legislation this afternoon in behalf of myself, Senator Bradley, Senator Simon and Senator Durenberger, and I will file my complete statement in the record as if read at this time.

[The prepared statement of Senator Kennedy follows:]

PREPARED STATEMENT OF SENATOR KENNEDY

Today, the Labor Committee considers the very important issue of direct student loans, and responsible ways in which the federal government should move in this direction.

The idea of direct student loans from the Federal Government that would be repaid through the tax system is not new, but it is receiving new interest because of the high cost of college education. As far back as 1954, Milton Friedman noted that such a plan would help students obtain the resources needed to invest in their future and develop their full potential.

In the 1970's, in a far-reaching proposal that gave new momentum to the concept, President John Silber of Boston University called for the establishment of a federal revolving loan fund, called the Tuition Advance Fund, which would combine direct federal lending to students with income-contingent repayment. Under this proposal, borrowers would repay, depending upon their economic success after they left college.

Working with Dr. Silber, I introduced this idea as Senate legislation in 1978. A year later, Republican Senator Henry Bellmon of Oklahoma and introduced a direct student loan program with some impressive support—including Senators Howard Baker, Thad Cochran, John Danforth, Pete Domenici, Jesse Helms, Nancy Kassebaum, Jim McClure, and Alan Simpson. So, if everybody still feels the same way, we ought to be able to enact this idea into law. Our 1979 legislation focused attention on the promise of direct lending. At the time, we chose to go the route of guaranteed student loans. But the growing problems and costs of that program have generated new interest in the direct loan approach. In the past year, several bills have been introduced in both the House and the Senate to establish a direct student loan program, and it now seems to be an idea whose time has come.

There are excellent reasons to move in this direction. First, according to estimates from the General Accounting Office and the Department of Education, a direct loan program will save substantial amounts over the current program.

Second, there is greater ease for both the borrower and the government. A direct loan program will have fewer middlemen and be easier to manage than the existing loan program. A direct loan program will be simpler for students and their families, and may well be much simpler for the Federal Government.

Third, income-sensitive repayment through the Internal Revenue Service will both streamline the repayment process for borrowers and allow graduates to choose employment after college without fear of being financially over-burdened if they choose lower income employment. Finally, by collecting through the Internal Revenue Service, we are likely to reduce loan defaults.

But just as there are reasons to move in this direction, there are reasons to move with care. Despite its many problems, the current Guaranteed Student Loan program serves millions of students a year and makes it possible for them to obtain a college education that might otherwise be beyond their reach.

In addition, a direct loan program will require the Department of Education to assume a number of new administrative functions that it is not currently performing. Despite improvements under Secretary Alexander, the department remains a thinly staffed agency with questionable ability to undertake major new administrative responsibilities, let alone perform its current responsibilities adequately.

Thus, we propose testing a direct loan program to gauge its benefits while being able to measure the government's capacity to administer it. The potential benefits of direct lending with income-sensitive repayment are too great to ignore. The two most important criteria in considering this initiative are: Is it better for students, and is it cheaper for the Federal Government? To both questions, the answer is yes and it is time for us to move ahead on this important and promising idea.

Over the past few weeks, I have met with other Senators who have expressed strong interest in this issue. We have designed a pilot initiative that will permit us to test the direct loan approach, with students repaying their loans through the Internal Revenue Service after they leave college.

Under our plan, which we are introducing today in legislative form, a diverse group of 300 schools will be chosen by the Secretary of Education to participate in Self-Reliance Loans—a supplemental loan program in addition to the current Pell Grants and Guaranteed Student Loans.

Schools will borrow the money from the Federal Government and make loans to their students. Any student at a participating school will be eligible for a loan. Students can receive up to $5,000 a year, with a total borrowing limit of $30,000. The money will be lent to students at an interest rate equal to the 52 week rate on

Treasury bills plus 2 percent. If the plan were in force today, students could borrow money at about 8 percent.

The loans will be repaid through the Internal Revenue Service by increased withholding. Before leaving college, borrowers will be given a choice of repayment options developed by the Secretary of Education and the Commissioner of Internal Revenue. Borrowers will continue to make repayments until the loan is repaid. After 25 years, any further indebtedness would be canceled.

The proposal includes important protection for borrowers. Before they receive a Self Reliance Loan, students must first apply for Pell Grants and Stafford Loans. To prevent students from borrowing too much, borrowers cannot receive more than the cost of attendance and borrow no more from all the federal loan programs than the total borrowing limits specified in the Higher Education Act approved by the Senate last week. To protect borrowers with low incomes, no repayments will be due in any year when a borrower owes no tax liability to the Federal Government.

This plan is intended to test the viability of the direct loan approach. If the idea works, I am certain that Congress will want to expand it to more schools and more students. If the test does not succeed, the program will be terminated.

But I do not expect the initiative to fail. There is growing support for this concept, and I understand that the Finance Committee will consider this proposal when it marks up the tax bill. I look forward to the hearing today to discuss the details of the plan and to identify improvements that may be needed.

At a time when tuition costs have been rising much more rapidly than family incomes, it is especially important that we do all we can to make college education more affordable and accessible to every young American. No investment is more important for the Nation's future.

I am especially pleased to have Senators Bradley, Simon, and Durenberger here today. Each of them is an effective advocate of this approach. The bills that they have introduced have brought new momentum to discussions of this concept. I look forward to hearing their testimony today and to working with them as we continue to develop this initiative.

Senator Hatch.

Opening Statement of Senator Hatch

Senator HATCH. Thank you, Mr. Chairman. I will file my complete statement as if read, also.

Normally under our rules, we have at least 1 week notice before we hold these hearings. Last week we were able to get the higher education bill through in 1 day mainly because this particular item was withdrawn from consideration.

I understand the desire to consider direct loans, but it is a complex issue and difficult to understand. I appreciate those who have made extra efforts to be here today on both sides of this issue, especially those who are against it, because they have had very little advance notice.

Let me just mention a few major problems that I find with this, although I'm going to try and keep an open mind. I'd like to see a better system. I'd like to see more opportunity. I'd like to see more young people benefit from our programs up here. But I think we need to look at this issue very carefully.

No. 1, this adds another new loan program to an already complex set of loan programs. No. 2, it makes an entitlement out of an untested program. Last week we had a discussion about entitlements in the higher education bill, and the entitlement aspect of the bill had to be dropped, and I would hesitate to add any entitlements to a budget that's already about 60-percent entitlement. That is one of the big reasons why we cannot resolve a lot of our budgetary problems today.

No. 3, it potentially shifts decisionmaking away from the Committee on Labor and Human Resources and toward the Finance Committee because of the collection by the IRS that will be required. That concerns me a great deal.

No. 4, many institutions, may not be capable of carrying out these new responsibilities or, if they are capable, this may add a great deal more paperwork and difficulties for them.

I have heard all the arguments that this will reduce paperwork and make a nirvana that we haven't reached before in the higher education system, but we all know that is never true in the Federal Government.

No. 5, the Department of Education may not currently have the capability to run this program.

No. 6, the IRS may not be capable of making the needed changes quickly enough with the tremendous problems that they have.

No. 7, I think there are a lot of questions that need to be answered, and I hope our colleagues will ask them in part here today. I have to leave because of a prior commitment that I had prior to notice of this hearing, which occurred only yesterday.

And No. eight, I think this program will encourage young people to go further into debt. That is a matter of great concern in this country today. We seem to think that everything should be free or that Government should provide. A lot of young people take that attitude and then get deeply in debt. There is no question that a lot of young people are deeply in debt today as a result of our current lending programs to students. It has added a tremendous amount of stress and difficulty to their lives.

I hope that you will answer many of the questions I have raised. I think they are a serious set of concerns. However, I am very interested, although the administration does not seem to be, in perhaps trying a pilot program or a demonstration project to see if this works. If it works, I'm all for it. But I sure as heck don't want to make a drastic change like this unless I know it works.

Did you want to comment, Senator Simon?

Senator SIMON. If I could just respond before you leave for that other committee meeting.

Senator HATCH. Sure.

Senator SIMON. That's what this is; we're talking about 300 schools.

Senator HATCH. That's a lot of schools.

Senator SIMON. Yes.

The CHAIRMAN. Three hundred out of 7,800.

Senator HATCH. I understand, but that's still a lot of schools.

Senator SIMON. But this is the first entitlement that you've ever voted for that will save money for the Federal Government.

Senator HATCH. And that will be the first time any entitlement has ever saved money. Nobody believes it will.

Senator SIMON. Well, don't take my word for it. Look at GAO, and ask CBO.

Senator HATCH. I'll be glad to do it, but I don't believe entitlements wind up saving money. I haven't seen any yet.

Senator SIMON. Well, this one does, because you are paying $3.2 to $3.4 billion this year on student loan defaults, and you will gradually reduce those student loan defaults. Second, on paper work——

Senator HATCH. If it works as you anticipate, I suspect—but they always said the other system would work that way, too.

Senator SIMON. Let me just add, on paperwork, take GAO's word for it if you want to or the College Business Officers. College Business Officers have gone on record saying this kind of program will reduce paper work for the institutions, and they favor it.

Senator HATCH. That's before the Federal Government gets the responsibility of implementing regulations. Once that happens, we all know we'll have more paperwork.

Let me just say, Senator—if you can answer every one of these questions, then I'll read the record and be interested in what you have to say. I have great regard for both of you as members of this committee and otherwise—but I am raising legitimate issues that have to be answered and which I think may cause people to be skeptical of a brand new, all-embracive program, even for only 300 schools—which I consider to be quite a few.

I'm really concerned about moving out of what we have, but I am prepared to do so if we can show that this is a better approach. I can support a new program if it will, in fact, save money. It will amount to better education for our young people and will not run them into tremendous debt and will not become a tremendous burden to the Federal Government, the IRS or anybody else. It also must not shift responsibility away from this committee and the Department of Education, which I think is very important here.

It seems to me if you're going to have a pilot project, you need a very carefully outlined pilot project. This bill, as I have read it, expands almost automatically to all schools by the year 1997. I would like to see a little more cautious approach.

Senator SIMON. If I could respond on that——

Senator HATCH. I know you're trying to help me, since I'm leaving.

Senator SIMON [continuing]. It expands to all schools only if Congress appropriates the money, authorizes it.

Senator HATCH. I understand that. But once these entitlement programs get into effect, and once you've got a lot of people depending on them, then Congress has to appropriate the money. We all know the game, and that's what happens around here. In fact, that's what makes entitlement programs so dangerous, because most of them are programs that really are critical programs to people. Once they get locked into an entitlement program it is almost impossible to make the necessary changes that will have to be made. You know that, and I know that.

That is why I think the administration is proper in being very skeptical, very concerned, and even downright opposed to any additional entitlements to our budget and to our budget process. Something will have to be done about that, before some of us can support this.

But be that as it may, I commend both of you and Senator Bradley for trying to apply some new ideas to something that could be done better. From that standpoint, I want to encourage you. I am going to continue to follow this and look hard at it.

I especially welcome the witnesses who are here today, especially John Silber, whom we have listened to before in the past. He is very innovative and creative and will be testifying for it. I also welcome Father Byron and others who are here including a representative of the Internal Revenue Service, who will have a lot to say about this program.

We are happy to welcome all of you here.

Mr. Chairman, I'm sorry to have taken so long. I appreciate having these hearings. I just wish we'd had a little more notice.

[The prepared statement of Senator Hatch follows:]

PREPARED STATEMENT OF SENATOR HATCH

Mr. Chairman, no one on the minority side is against a fair and thoughtful review of the pros and cons of a direct loan proposal. It seems that anytime we have had a hearing on a direct loan proposal that we have done it on a rush basis.

Last week we were confronted during the floor debate on the Higher Education bill with a direct lending proposal that seemed to change on an hourly basis. Trying to get a handle on this proposal was like trying to hit a moving target. Moreover, for such a complex proposal involving billions of dollars, hearings on the feasibility of this approach were, in my view, inadequate and not comprehensive.

It is no wonder the people's confidence in their public officials is so low when we give them such awful examples of the legislative process in operation.

I realize the chairman is trying to rectify this deficit of knowledge with this hearing today. But, in doing so, he has violated certain rules of process that make for a more orderly, comprehensive, and fair learning environment for Senators.

Rule 8 of our committee rules states that notice of a committee hearing must be given at least one week in advance. The rationale for this rule is evident. It permits Senators to reserve time to attend; it allows time to secure witnesses and for those invited witnesses to prepare testimony. Ideally, we ought to have more than 7 days notice.

But, Mr. Chairman, this hearing has been thrown together. The official notice of it arrived only yesterday morning. With all due respect to our witnesses—and I sincerely appreciate the fact that they have done us the favor of dropping all of their other commitments to be here today—this has hardly been a thoughtful and deliberative process.

I certainly hope this method for scheduling meetings of the committee will not become the norm.

I think all of us have listened to the many claims made by the proponents of direct loans. It is difficult not to be swayed by the arguments in favor of reducing defaults in the student loan program and of saving taxpayer dollars. However, we need to make sure that these claims are not inflated expectations that ignore many of the additional costs and potential problems involved in a direct loan program.

We passed the Higher Education Reauthorization Act last Friday in the Senate with only one dissenting vote and in only one day, largely because the proponents chose not to offer their amendment for direct lending on student loans. This proposal did not have adequate support last Friday because too many questions remain.

As I see it, there is plenty of time to review this proposal more adequately. The House has not yet passed its bill for Higher Education. Why then does the Senate need to rush this bill through without adequate consideration?

It seems to me that this freight train is moving down the track a bit too quickly. There simply is no deadline that is forcing us to rush this bill through a process which is designed to allow the kind of deliberation necessary for a change of this magnitude. If this proposal is such a great idea, it ought to be able to withstand the scrutiny of closer examination by all parties involved in the current student loan program. I have always believed that if an idea is not a good idea tomorrow, then it is probably not a good idea today.

I can assure you that I am as eager as anyone else on this committee to reduce the cost of the student loan program. But, in that process we must not destroy the student loan program and limit the ability of our students to obtain the higher education that is so vital.

I also wonder why we want to enact a new bill that provides another entitlement program. As I recall, the Senate last week decided to eliminate the Pell entitlement provision from the Higher Education bill because we simply could not afford to create a new entitlement even out of a program that has been tested and tried for many years and is a program that enjoys broad support. How can we justify entitlement status for a direct loan program, which has never been implemented anywhere and which has not withstood the test of time?

This is not to suggest that we should not investigate a direct loan proposal responsibly. While I hope to get some questions answered at this hearing, I am not sure that a hastily called one shot hearing will be sufficient.

Again, I appreciate the testimony of our witnesses who have come before us with minimal notice. I especially want to thank the witnesses who have come to express their reservations about this program, since they have had even less notice than the advocates.

Despite the haphazard nature of the way we have considered this issue, I want to assure our witnesses and those who are visiting today that the committee is sincerely interested in your views, which are vital to us in fashioning a common sense, workable approach to financing and administering student loans.

The CHAIRMAN. Senator Pell, the chairman of our Education Subcommittee.

Opening Statement of Senator Pell

Senator Pell. Thank you very much, Mr. Chairman, and I must apologize for coming in and out. I am presiding over the Foreign Relations Committee just down the hall.

As I have said on several occasions, I am very interested in the concept of direct loans, of income-sensitive repayment, and of IRS loan collection. All are concepts that I believe have merit and should be tested.

Following so close on the heels of Senate passage of the Higher Education Reauthorization bill, I believe I would be remiss if I failed to impress upon my colleagues my reluctance to support creation of a nonneed-based loan entitlement when we put off bringing full entitlement status to the Pell Grant program.

To do something for well-off families at the expense of needy and deserving ones could be, to my mind, a mistake. It is even worse if we do so by favoring loans over grants. We did not do that in the higher education bill, and we should not do it here. Both the poor and the middle-income have very real needs, and both deserve our help.

Further, as we look at the Bradley-Simon-Durenberger proposals which, as I have said, have real merit, there are several provisions that I believe must be an integral part of any program of this nature.

First, it should be done on a pilot, test, or demonstration basis. It should have a beginning and a termination, clear and simple. Provision should also be made for a study of the program near the end of the test so that we will have the necessary information on whether to move ahead.

Second, it must supplement and not supplant the existing student aid programs. A student applying for a self-reliance loan should first apply for a Pell Grant and a GSL. We must make sure that the student receives the aid that is most favorable to his or her particular circumstances.

A grant is far more preferable than a loan, and a GSL is more preferable than a self-reliance loan.

Third, the amount a student can borrow under the self-reliance program should be subject to some of the overall limits placed on borrowing as provided in S. 1150 passed by the Senate last week. This limits undergraduate borrowing to $52,000. Placing the self-reliance program within these limits ensures that poor students will not over-borrow, and that is critical.

Fourth, if a student has both a self-reliance loan and a GSL, both loans should be subject to collection by the IRS. To do otherwise would be to place a priority on the payment of self-reliance loans and relegate GSL's to second class repayment status after self-reliance loan payment has been taken from a borrower's paycheck. I believe such a situation could lead to a serious increase in GSL default costs.

Finally, any demonstration should involve a limited number of schools. The original proposal contained 500 schools, and I believe it should be half of that.

These are all provisions that I believe should be included in any demonstration bill. Most important, however, the legislative language must be clear that the program is only a demonstration or test, and the language must be straightforward in that regard.

I would close by saying that while the idea has real merit, I think it should be wedded to these guidelines, and then it will be worthy of support.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Pell, for your very constructive suggestions as always.

Senator Kassebaum, the ranking minority member on the Education Subcommittee.

OPENING STATEMENT OF SENATOR KASSEBAUM

Senator KASSEBAUM. Thank you, Mr. Chairman.

First, because the 1979 bill has been mentioned several times, I would only make note that one of the reasons behind the 1979 bill was that banks were very reluctant to get into the GSL program, and this was designed to help encourage them to make those loans. Now, of course, the proposal is to take them out, just to note how things do change.

I think all of us are concerned about the situation, but I worry about how we tend to gloss over some of the difficulties that are involved. We want simplification; we want to make loans more available. We all want those things. Of course, colleges and universities have quite a stake in this as well as, as has been pointed out, the lending institutions. But I think we should look at some of what I think are the profound implications of this proposal. They have been touched on a bit already. I think Senator Pell raised some very good points, and I would like to reiterate a few.

I don't accept the notion that the concept behind the existing loan programs is totally flawed. These programs leave banks in the banking business rather than making the Federal Government the banker. I think that we might end up, if we look back on this 10 years from now, wondering why in the world we thought the Federal Government would be a better banker.

On the other hand, the Guaranteed Student Loan isn't perfect. I think that what we need to do, frankly, is to spend more time analyzing the merits of different means of approaching this issue.

In fact, I understand this bill was just submitted at 6 o'clock last night. It has been through various revisions in the last 5 days. I think it will benefit us to consider it far more carefully, because I think it has great significance.

Much has been said here about its being a demonstration project; it applies to only 300 schools. But the trouble is, as Senator Pell pointed out, it doesn't end. A demonstration project has a termination point, at which time you analyze that demonstration. I think if we want to call it a demonstration, we have to put that in the bill.

Second, there has been talk about creating a new entitlement program, as this does. I think it is inviting serious budgetary problems in the future, on top of those we face today. We are just continuing to add on without thinking about what we can subtract.

This adds a loan program to those we already have; it doesn't take anything away. So it is a new entitlement on top of an entitlement.

We have in the higher education reauthorization just passed by the Senate opened up the supplement loans for students (SLS) program so that it could go to creditworthy dependent students. I wonder if it would not be perhaps wiser to look at expanding further the SLS initiative rather than adding this new loan program, which essentially would reach those SLS students. I don't know if any thought has been given to this, but it seems to me that may be a more practical approach.

Third, there are numerous practical problems which would have to be addressed in the establishment of a workable program—one being determining the administrative and financial capacity of institutions to take on such a program. Perhaps this issue will be addressed by the presidents of some fine institutions in their testimony today—as far as their being able to take on some of this red tape.

When we talk about red tape, the administrative requirements of institutions are not going to be reduced by this new program. In fact, they may well grow because they are going to be having to submit monthly lists of borrowers, reporting changes in enrollment status, and transferring promissory notes. I'm sure there are going to be many more things we haven't thought of yet.

Determining the capacity of the Department of Education to undertake supervision of an entirely new loan program, while administering all of the other existing aid programs, is another important issue. That's why I say we're just adding to what we're already doing.

The department is undertaking a long-needed revamping of its management of student aid programs. I think it is ironic to consider that, at the point when some of the improvements are starting to show results, we would be initiating a whole new set of potential problems. This proposal calls for the department to conduct extensive tracking of self-reliance loan borrowers to calculate their loan obligations, to establish a process for resolving disputes regarding those obligations, and to devise repayment options and report all of this information to the Internal Revenue Service.

Now, that's a long list of new requirements. In addition, the Internal Revenue Service will have to revise forms, instructions and withholding tables and to otherwise undertake collection activities which go far beyond its reason for being, which is the collection of income taxes. One could argue they've perhaps gone way beyond that reason for being already, but I think that this is moving them into a whole new area.

Moreover, at a time—and Senator Hatch touched on this—when we worry about the accumulation of consumer debt, we are making it as attractive as possible for students to borrow even more. I find it really tragic to visit with students who are out struggling to find jobs, just as you mentioned, Senator Durenberger, or who reciev paychecks that don't begin to be commensurate with the debt they have undertaken. Perhaps the fault is not theirs, but ours.

We hear there won't be any default rate. Well, no, not per se. Does this mean that, just because students haven't been repaying their loans, all of a sudden they will because the loans that are going to be collected by the IRS? Or, does it mean that perhaps there would be tax evasion or, after 25 years, forgiveness?

I'm not sure that we can say that somehow defaults will disappear. We all know how many defaults have been accumulated. We cannot afford to lose the ability to check those institutions that have high default rates. I think frankly all of this must be considered.

Mr. Chairman, there are many things to be discussed and many questions I would like to ask the panelists, but those are just a few of my concerns. I would like my full statement to be made a part of the record.

The CHAIRMAN. It will be made part of the record.

[The prepared statement of Senator Kassebaum follows:]

PREPARED STATEMENT OF SENATOR KASSEBAUM

Mr. Chairman, last week the Senate approved legislation reauthorizing the Higher Education Act. That legislation was the product of well over a year of hard work on the part of this committee, and it was adopted by the full Senate with only one dissenting vote.

I believe the overwhelming support for this legislation was warranted, as it made significant steps towards strengthening program integrity, simplifying the process, and expanding aid to students. Having put enormous effort into the development of that bill and having just spent two days on the Senate floor with it, I find it somewhat disconcerting that we are today going back to the drawing board to second-guess decisions made months ago.

I would also like to register my strong objections to the scheduling of this hearing in violation of committee rules which require that members be notified at least one week in advance of any committee hearing. The requirement for timely notice permits members to prepare for the hearing, to plan their schedules so that they may attend, and to permit adequate time for the selection of witnesses who can properly address the issues being raised. Receiving word over the weekend of a Tuesday morning hearing effectively provided less than 24 hours in which to accomplish these tasks.

I trust that this situation will not be repeated in the future, as it is detrimental to the orderly consideration of committee business and is a poor mechanism for arriving at sound policy judgments. Having said that, let me express my particular appreciation to those witnesses who—with even less notice than members of the committee received—were willing to adjust their schedules to provide testimony today.

It is my view that the proposal we are considering today has arrived far too late in the process. Certainly, the general concepts of direct lending, income-dependent repayment, and IRS collection have been around for some time. However, the specific bill which I understand we are addressing today has been available only since about 6 p.m. last night.

Moreover, we have never gone beyond the surface appeal of these notions. The substantial philosophical, budgetary, and pragmatic problems with them have been either glossed over or lightly dismissed as being the self-serving cries of vested interests. The debate over a proposal with profound implications in areas including student indebtedness, college costs, federal debt and obligations, and the integrity of student aid programs deserves far better than this.

Let me lay out more specifically some of these concerns:

First of all, I do not accept the notion that the concept behind existing loan programs is fundamentally flawed. These programs leave banks in the banking business rather than making the Federal Government the Nation's banker. Obviously, the guaranteed student loan program is not perfect, but we should be under no illusion that a direct lending program would be. Past budget bills, as well as the legislation just approved by the Senate have been aimed at learning from experience in order to fix the problems which have emerged.

Second, creating a new entitlement program—as this proposal does—is inviting even more serious budgetary problems in the future than we face today. No financing mechanism is either identified or required by this legislation. Mandatory spending programs in combination with annual interest payments on the federal debt already consume over 64 percent of our budget. We simply cannot continue locking ourselves out of future spending options.

Third, there are numerous practical problems which would have to be addressed if any semblance of a workable program is to be established. These include:

Determining the administrative and financial capacity of institutions to take on a program which has them originating loans, submitting monthly lists of borrowers, reporting changes in enrollment status, transferring promissory notes, and counseling borrowers on complicated income-tax-based repayment options.

Determining the capacity of the Department of Education to undertake supervision of an entirely new loan program, while administering all other existing aid programs. The department is undertaking a long-needed revamping of its management of student aid programs. It is ironic to consider that, at the point when some of the improvements are starting to show results, we would be initiating a whole new set of potential problems. This proposal calls for the department to conduct extensive tracking of self-reliance loan borrowers, to calculate their loan obligations, to establish a process for resolving disputes regarding those obligations, to devise repayment options, and to report all of this information to the Internal Revenue Service.

Determining the capacity of the Internal Revenue Service to revise forms, instructions, and withholding tables and to otherwise undertake collection activities which go far beyond its reason for being (the collection of income taxes). It is my understanding that it would take a minimum of 5 years for the agency to be in a position to assume such responsibilities. At the same time we are making every effort to simplify student aid forms, we would be creating a nightmare for any borrower trying to submit a W-4 form or decipher a 1040.

Moreover, at a time when we worry about the accumulation of consumer debt, we are making it as attractive as possible for students to borrow even more. The notion of paying up to 7 percent of one's adjusted gross income for up to 25 years after graduation is an abstract notion at best to an 18-year-old entering college. This proposal makes no recognition at all that families able to do so should contribute to the education of their children.

It makes it easier as well for colleges to raise their costs. Serious questions are raised as well regarding the impact of this proposal on program integrity measures which rely on default triggers.

In short, I do not believe we are anywhere near being in a position to start up a new loan entitlement program. The questions I have raised are serious ones which are not going to be addressed in a 2-hour hearing put together with a few days' notice. New ideas are fine, but let us not forget that any idea requires careful thought and planning to be put into successful practice.

The CHAIRMAN. Of course, the Senator knows the limits on borrowing that are established in the higher education bill will be consistent with this legislation. It always amazes me that the IRS can withhold on the number of dependents that you have, where you have evolving and changing families; and to do it over the projection of percentage of a person's income over the period of a lifetime would present more complicated factors, it seems to me. But these are the kinds of things I guess we'll have to look at.

Senator KASSEBAUM. Mr. Chairman, I don't mean to get into this at this point. You're right—the overall borrowing limit remains the same. But that's why I asked the question——

The CHAIRMAN. That's right, with the one exception of the independent students that we provide, but that's a small percentage.

Senator KASSEBAUM. That's right.

The CHAIRMAN. But that's why this has been an evolving process to tie that into the existing programs with the overall limitations, and also for the reasons that you and Senator Pell have mentioned, so that a student will know his or her eligibility in terms of the grant program, the GSL program, before they get into this and the various financial considerations, because obviously GSL has a subsidy. We have tried to do it.

And I want to say to the good Senators here that this is going to be a continuing and evolving process.

Senator DURENBERGER. Mr. Chairman, I just want my colleague from Kansas to look at the chart that my colleague from Illinois produced. That is the heart of the current problem. All of those young people you're talking to out there are stuck with those loans above the line, and they can't make the payments and can't make other decisions. And the hash mark under it is called income-dependent loans. That's the big difference.

Senator COATS. If I could just interrupt here—I know we're getting a little more free flow here than probably we should—but if they cannot now pay the existing loans, what makes you think that an additional loan on top of the ones that they can't currently pay is going to be paid? I understand that the IRS might have more leverage in terms of collection—although there is some testimony here from the IRS that shows some real concerns about their ability to collect these—but if the students are currently having that much trouble paying existing loans, how are they going to have less trouble adding another layer of indebtedness on?

Senator DURENBERGER. If I may, Mr. Chairman, say to my colleague from Indiana, unfortunately, having once come up with an argument like that, which is to substitute the hash line for the thick line, we are now faced, because of the situation we find ourselves in, with having to answer the argument why are you layering on top of a layer—we don't intend to layer on top of a layer. We intend to provide people in the future with a new and different alternative. The alternative to borrowing GSL and ending up owing more than you can afford to pay is to borrow through self-reliance and have an affordable payback that adjusts to your income.

Senator SIMON. If I could add, students would choose, and the students would choose, I believe, in most cases the loan that is income-contingent.

Senator COATS. But under this program the students could choose both; isn't that true?

Senator SIMON. It is theoretically possible that they could have both. They are limited; the loan limits here don't change. But that is possible, and I think it is one of the practical things we have to deal with.

If I could just respond to Senator Kassebaum's comments, because I think that really gets to the heart of much of this—how can we be sure that we are reducing and eliminating the defaults. We are doing it in two ways. One is the IRS collection, and the second is you take Treasury rate plus 2 percent. So, like on the Lockheed and on the Chrysler loans, that 2 percent is a cushion, and the estimate is that that will more than take care of any defaults that we have.

So I think you really do eliminate the defaults for those who take this particular loan.

The CHAIRMAN. I'm going to recognize Senator Bingaman so we can get through our opening statements, and then we'll get on with our panels.

OPENING STATEMENT OF SENATOR BINGAMAN

Senator BINGAMAN. Thank you very much, Mr. Chairman. Let me compliment you for the leadership you have shown over a long time on this issue. I was not here when you proposed this back in the Seventies, but if I had been, I would have cosponsored it.

I did cosponsor Senator Bradley's proposal when he introduced it earlier this last year, and I compliment him and Senator Simon and Senator Durenberger also for their hard work on it.

Let me just address two or three of the points that have been discussed. The issue of this being a new entitlement—that phrase is used to cover a world of different things. As I understand this proposal—and let me just ask the sponsors if this is right—there is technically an entitlement as regards students who attend the 300 schools that the Secretary would choose during this 4-year period, or for this pilot which would last for 4 years, but the Secretary is directed to choose those schools on the basis that projected volume of new student borrowing would not exceed these figures—$450 million for the first year, then $550 million, then $650 million, and then $900 million. So that conceivably he could miss those targets, but that is clearly our intent, and it's not likely he would miss them by much.

Senator SIMON. That is correct.

Senator BINGAMAN. And after that, there is no entitlement the way I read the bill. After that, Congress has to provide sufficient resources to offset the cost of the income-dependent educational assistance program if it is to be expanded.

Senator SIMON. That is absolutely correct.

Senator BINGAMAN. So that I don't think there is an entitlement after those first 4 years—now, maybe I'm misreading it, and if I am someone needs to correct me—but as to the 300 institutions, there is an entitlement. The Secretary's ability to go beyond the 300 is limited on page 5 to the condition that Congress must in fact take the affirmative step of approving the expansion of the program by providing sufficient resources. And that's your understanding as well?

Senator DURENBERGER. Yes.

Senator BINGAMAN. Let me ask about the 4-year period because I have a little bit of concern. I think Senator Hatch said that he was worried that 300 was too many schools. I'm worried that you might be providing a very substantial benefit to those 300 schools in the recruitment of students which other schools might not have. In my State, for example, we have several very good institutions of higher education, and for example, if the University of New Mexico were chosen as one of the 300 schools, and New Mexico State University were not, or vice versa, would the student who is determining which of those schools to apply to have a tremendous incentive to apply to the school that had been chosen by the Secretary? I would be interested in either Senator Simon or Senator Durenberger responding to that concern.

Senator SIMON. I think the honest answer is there is some incentive there, and I don't know how you deal with that without making the program universal. So we are simply going to have to have an experiment where some schools temporarily may have a slight advantage. But I don't know how you get away from that.

Senator BINGAMAN. Let me ask on another related point, in the selection of schools on page 4 of the bill, it says that the Secretary shall choose these select institutions, and then it gives a series of criteria. It says "a cross-section of institutions" shall be chosen "by educational sector, length of academic program, default experience"—now, that one sort of stops me. Is the idea that we want some schools with high default rates as well as schools with low default rates?

Senator SIMON. I think it's the opposite. We want to reach a variety of schools, but obviously if a school has a very high default rate, that school is not going to be high on the priority to be named one of the 300 schools.

Senator BINGAMAN. I would just suggest that maybe that's an item that you could look at in the drafting, because the way I read it, it seems to call for the selection of a cross-section of institutions according to those criteria, and if you get a cross-section of institutions based on their default experience, I don't know if that's what you intend.

Senator SIMON. No.

The CHAIRMAN. Senator, that is further refined and clarified at the top of page 19, where it reads: "the term 'institution of higher education' means an institution of higher education which has demonstrated the administrative and fiscal capacity to carry out the provisions of this part." We try to clarify it there. But we'll certainly take up the suggestions.

If I could just say, for those schools, there may very well be a marginal advantage, but they are under the overall borrowing level, which I think makes a difference.

And just to say—and I didn't mean to interfere—but I think it is enormously important since the word "entitlement" is such a buzzword. I always like to hear it when people complain about it which entitlements they want to repeal. In terms of the cost of this program, it is about $30 million a year subsidy, effectively, for the period of the first 4 years or 5 years of the legislation. That's the extent of it. And I hear what you are saying; that issue has to be addressed under the budget agreement with either a designated tax that is going to be specific, or otherwise a reduction in another entitlement program. We understand and are working with the Finance Committee to deal with that very issue. I think it is worthwhile just to raise the point, but we ought to put it in some perspective as well. The issue has been in conversation, and it hasn't been satisfactorily disposed of in terms of the Appropriations Committee today, but there have been active and continuing discussions with the chairman of the Appropriations Committee, and that is going to be an ongoing process. I think it is important just for the basis of the record to understand where we are.

I apologize to my friend from Indiana.

Opening Statement of Senator Coats

Senator Coats. Mr. Chairman, first of all, I want to compliment Senators Simon and Durenberger, and Senator Bradley who is not here, for taking the step to look and see if there is a better way we can do something. Too often we don't do that. We put a program in place, and we assume that it is there, and therefore that's all there is. And you have attempted here to construct a better mousetrap—I don't know that we know if it works better yet or not, but at least you are making the effort, and I compliment both of you on that. And I hope we can have some substantive, serious debates and discussions about whether or not it is a better mousetrap and is something that we ought to pursue.

Clearly, I think everybody in this room would support the goals outlined by Senator Bradley. We do want to provide access to higher education to as many Americans as we can. We know that the costs are excessive and that education is being priced out of the range of a lot of Americans and their families. We do believe that higher education is ultimately a benefit to our economy and to our Nation.

Those are all desirable goals. As we examine how we get there, I would hope—and while it is not within the scope of this committee—I would hope we wouldn't just pass over the question of why these costs keep rising. That's like addressing health care and saying, well, there is nothing we should do about the increase in costs; let's just see if we can keep providing people with enough money pay for these costs.

The increases in higher education, for whatever reason, are exorbitant; they are going beyond people's ability to pay. And as we look at those increases and as we look at the way some of the funds are being spent and so forth, I think some very serious questions have to be asked of the institutions as to what they're doing to try to hold down the costs because we're never going to be able catch up. Given our current debt, given our obligations that are already on the books, we are never going to be able to catch up in terms of providing assistance to students and families to pay for higher education if the costs keep rising at double-digit rates.

I am sympathetic with the problems faced by the colleges and universities, but they'd better take a look at their own shop if they expect to keep attracting students and providing education.

By the same token, we need to look at ways that we can assist them. I obviously share the concerns raised by Senator Hatch, Senator Kassebaum and others relative to where we're going with this program.

I think the history of entitlement programs is that early on the discussion was exactly what we are talking about today—it's going to cost so much; we can't go beyond this; Congress doesn't authorize it or appropriate it; we won't spend any more than "x" amount of dollars. But we all know how entitlements work. We all know that once a program gets on the books, a tremendous political consensus or constituency arises in support of it, there is a lot of pressure on Congress, and we are here assuming that a program has to be funded and funded at increased levels, and we begin to talk about the number of students who aren't eligible for the money, and after all only 300 schools participate, and why shouldn't 3,000 participate—and on and on and on, and it grows to the point where we seem not to be able to exercise the political discipline to hold down the costs.

I am wondering about the language here in the bill that is introduced which says in section 453, "an eligible student at a participating institution shall be deemed to have a contractual right against the United States to receive a self-reliance loan." I'd love to be a lawyer handling cases for students, if Congress didn't appropriate the money after we guaranteed them a contractual right in the law to receive the money.

So I don't think we can simply say that we'll look at this in 4 years, and if it doesn't work as well as we think, or if we don't have the money to pay for it, we're going to nullify the contractual rights of those students. I'm not sure that we are going to be able to successfully do that.

And I think we need to be careful in terms of how we use statements relative to IRS collection and CBO analysis of this. The testimony given in February before this committee by Michael Bigelow, deputy assistant commissioner of the International Revenue Services, says, "the collection of delinquent student loans would add to a very sizable existing accounts receivable inventory. While a portion of this accounts receivable inventory is made up of accounts which we hope to collect in due course, 27 percent of the inventory is composed of cases which we categorize as currently not collectible. These cases include bankrupt taxpayers, taxpayers who can't pay because of hardship, and taxpayers that we cannot locate. We

53-314 O - 92 - 2

believe that many of the delinquent student loans which cannot be collected through the offset program will fall into this category."

Now, look, we're going to have students who on the front end are going to sign up for a guaranteed $30,000, who are going to be making a judgment at the age of 17 or 18, saying, "Sure, sign me up. I'll pay it back, because I'm going to be making $100,000 after I graduate, and jobs are going to be available for me." We are going to have a lot of students where those jobs might not necessarily be available, or at least at the rate that they thought, and they are going to fall into this hardship category or be advised to take bankruptcy.

So to assume that we are going to collect all those loans, and it is going to just flow into the Treasury to create a revolving fund I think is an assumption that needs to be examined.

Then finally, the CBO report, while it does discuss possibilities of providing savings—and that's what we would all like—more money for more students—it says, "while it seems likely that subsidy rates will be lower under the IDEA program, the amount of borrowing will almost surely be greater. First, many potential borrowers may find the new program much more attractive than the fixed repayment required under Guaranteed Student Loans; second, loan limits will be higher, and finally, IDEA loans will be available to all families of eligible students, without regard to family income.

Even though the subsidy per dollar will be lower for IDEA loans, total subsidy costs could prove higher if borrowing increases substantially."

Clearly, there is going to be a very substantial period under a 25-year loan repayment program in which a lot more money is going to be going out than is coming in. A lot of up-front money is going to have to go out until that first student graduates from school, takes a job, and begins repaying 5 or 7 percent of their income back into the fund.

So we are looking at a substantial amount of additional borrowing against a Government account which most people would conclude is substantially over-borrowed already. And to pretend that there won't be substantial interests costs to the American taxpayer in the meantime I think is not looking at the situation realistically.

These are some of the questions that I think need to be examined. I don't have all the answers. I am glad that we're looking at it. I hope we take a serious look at it. I hope we don't rush to judgment here in a political year, thinking this is something that we can shove out there to a hurting middle America and then find ourselves 4 or 5 years from now in a bigger mess than we currently are in.

The CHAIRMAN. I'll now recognize Senator Thurmond.

OPENING STATEMENT OF SENATOR THURMOND

Senator THURMOND. Thank you very much, Mr. Chairman.

Mr. Chairman, I want to commend you and Senators Simon, Durenberger and Bradley for your efforts to improve this situation. The question in my mind, however, is whether this will improve it.

For instance, in South Carolina, all the colleges and universities we have heard from are unanimously opposed to this proposal.

Most view it as an added burden for their financial aid administrators, who are not equipped to handle such a program. They indicate there are too many unknowns with such a proposal.

The South Carolina Student Loan Corporation, which administers the loans in my State, is opposed to it as well.

Mr. Bill Mackie, the executive director of a nonprofit corporation, has written a detailed letter, and I won't go into all of it, but I would like to mention that he strongly opposes direct loans and has also called on different occasions on this issue. He suggests that the capital outlays to start up a direct loan program would be substantial and would add substantially to the Federal deficit. In addition, he suggests neither the Department of Education nor higher education institutions are equipped to oversee and administer such a program. And one final point that he makes is that those with lower incomes will end up paying far more under the direct loan proposal because it goes as far as 25 years, because the person pays less each year, and the payments are stretched out over a longer period with interest accruing all the time.

Then the Department of Education is strongly opposed to it because of the cost concerns and because of concerns about the ability of the Department of Education to administer such a program.

Now, these are a few points in opposition to this program that I think are worth noting. Direct lending represents a radical departure from existing law, and there are too many unanswered questions about how it will actually work out and whether it will really work as the proponents suggest.

Under the direct loan plan, the Federal Government absorbs all the losses from student loan defaults. Under the current law, the losses are shared by the State guaranty agencies and the Federal Government.

The Department of Education and many higher education institutions are ill-equipped to administer such a program.

With a 25-year payback period it could hurt rather than help those, as I mentioned a moment ago. With 7 percent of our adjusted gross income going for payments, it will take a long time for many to pay off huge college debts with interest accruing all the time.

The Federal Government would fund the start-up capital costs, which would add significantly to the deficit until students began paying back loans through their tax returns. The discussion draft calls for a projected volume of new student borrowing of up to $450 million in fiscal year 1994.

The Congressional Research Service, the research service within the Library of Congress that helps the Congress, indicates a big unknown in new administrative costs for the Federal Government for originating and collecting student loans. Repayments will not offset the debt for many years.

Nearly all the colleges and universities, as I understand, have made a report on this and seem to be opposed to it. I understand the GAO made a favorable report, and there are points in favor of this, but it seems to me the preponderance would be against it, certainly at this time.

I want to mention, too, that this is a new entitlement. There is nothing that has done more toward getting this country into the debt it is today than entitlements. Fifty or 60 percent of the debt is because of entitlements. Are we going to add another entitlement?

Today, as you know, the Federal debt is $3.8 trillion, and the projected deficit for this year alone, 1992, is $362 billion. I think we'd better be more cautious, and we don't have to act on this matter at this time. I think we had better consider it further.

Now, there was something said about Senator Kassebaum and Senator Cochran changing their minds. Well, fools never change, but wise people do.

That's all, Mr. Chairman. I've got to leave, but I would ask unanimous consent that my basic statement come ahead of the statement I made in the record.

The CHAIRMAN. It will be so included in the record.

[The prepared statement of Senator Thurmond follows:]

PREPARED STATEMENT OF SENATOR THURMOND

Mr. Chairman: It is a pleasure to be here this morning to receive testimony on the latest proposal to provide for direct student loans. Last October this committee had a hearing on direct lending and received testimony from several witnesses including the Deputy Secretary of the Department of Education, the Director of the Congressional Budget Office, representatives of the General Accounting Office, and representatives from the college community. Then, as now, it was obvious that this is a highly contentious issue over which there are great differences of opinion. A few months went by, and then last week we considered the higher education bill on the floor of the Senate. No amendments on direct lending were taken up, and in the final analysis, we ended up with a good bill which passed by a vote of 93-1. It seems a bit unusual to now go back and hold more hearings on this issue.

In any event, I am concerned about the process as well as the merits of the proposed direct lending draft. While some of the concepts posed by direct lending have been thought out and debated in some circles, there are many unanswered questions:

What is the status of the existing Department of Education income contingent pilot program established in 1987? Is it working? Is it efficient and effective?

In a practical sense, given past history, is the Federal Government capable of efficiently handling such an undertaking?

Is direct lending really likely to work better than the existing system of having the private sector make the loans, and the Federal Government guarantee them?

What about the initial large outlays by the Federal Government to get the program started—what impact will this proposal have on the total Federal debt?

And does such a proposal pose additional burdens on college financial aid offices?

Mr. Chairman, these are just a few of the questions posed by direct lending which I believe are worthy of close scrutiny. I join in welcoming the witnesses and look forward to their testimony.

The CHAIRMAN. I would point out that this is a voluntary program, Senator, so none of your colleges or universities have to worry about it. If they don't want it they don't have to volunteer, and it will mean more money in other parts of the country. I know there are people who have been trying to hard to bang away at Social Security as an entitlement, and if people want to work at that, they will have their opportunity to do so.

Senator Jeffords.

Opening Statement of Senator Jeffords

Senator Jeffords. Thank you, Mr. Chairman.

Certainly I want to commend the Senators before me and also Senator Bradley for bringing this issue up. I think this is an opportune time to start discussing new ways to try to finance our postsecondary education.

However, I would point out that I think it is a little premature to get too seriously into any kind of a system before we review the whole situation. This is probably the first time in 60 years that we will have an opportunity to take a look at our national priorities and reorder them, and that is very, very important. Certainly, education overall has to be at the top of the list of that which will get attention with expanding funding and work.

In the 1986 reauthorization, I got a commission established to study these very questions, and they are now meeting and going to be reporting at the end of this year on various options to change the future financing of postsecondary education.

We also have the National Voluntary Service Act to take a look at. I think there are some very excellent options available in that program, to assist us in finding ways to reduce the amount of loans necessary for today's postsecondary education. I think we have to take a look at the military and whether that can be reformed, especially with respect to taking up some of the problems we have with skill training and so on. So it is time that we take a look at it.

And I'm not afraid of entitlements. As you know, I was willing to sponsor an amendment of Senator Pell to make the Pell Grants program an entitlement. But I do have some serious concerns about phasing in a direct loan program at this time. I don't have a problem with a small demonstration project, but I'm worried with one that ends up as an entitlement before we have fully analyzed and taken a look at the other options that are available. Mr. Chairman, I'm pleased to be here today.

The Chairman. Thank you very much. To my good friends and colleagues, if you'd like to make a very brief comment——

Senator Simon. Very briefly, Mr. Chairman. Congressman Tom Petri would like to enter a statement in the record.

The Chairman. Fine. It will be included.

[The prepared statement of Mr. Petri follows:]

Prepared Statement of Mr. Petri

Mr. Chairman: In the United States, we have the pre-eminent system of higher education in the world. This is important if we and our ideals are to stay competitive in an ever changing world. As Members of Congress and public servants, it is our job to maintain our pre-eminence, and to make certain that all Americans have access to the system.

That is a challenging mandate, and I applaud this committee's willingness to consider new approaches such as income dependent lending as advocated by Senators Simon and Durenberger, among others. I am convinced that the Income-Dependent approach, which many of us refer to as IDEA, offers the fairest and most efficient way to help students finance investments in higher education.

IDEA is a direct student loan program, in which repayment is based on the borrower's income after school, and is collected as personal income tax by the IRS. The basic principle behind IDEA is that education represents, at least in part, an investment. Students are investing in human capital, and they expect a return on that investment in the form of higher future incomes. Under IDEA, the government backs such investments in human capital and in exchange receives a participating interest in the returns to that capital. In effect, students borrow against their future income streams.

On an individual basis, students can't finance education in this way, because they can't pledge their human capital as collateral and each individual can't guarantee a particular level of return on his or her investment. But collectively financing education on the basis of pooled risk and return on investments is a sound governmental approach to student aid. IDEA takes that sound approach from theory to practice.

When we do that, it turns out that this approach enables us to achieve a large number of important advantages. In the first place, IDEA is clearly fairer than the Stafford loan program. IDEA repayment is geared explicitly to ability to pay, whereas Stafford is actually regressive. Under Stafford the students who stay in school for the longest time, and therefore have the highest later incomes, pay the lowest effective interest rates on their loans because they get the most benefit from the in-school interest subsidy.

A second major advantage of the IDEA approach is that it provides a better deal than Stafford, SLS, or HEAL for most students. For most students in 4-year programs, the cost of IDEA loans is approximately equivalent to that of Stafford, but the IDEA loan provides the added advantages of insurance against low income, ease of repayment through the income tax, and complete flexibility of repayment that accommodates life changes like unemployment, periods of child rearing, divorce or death of a spouse, low earnings right after school, or periods of low wage public service employment. For shorter term students, IDEA is a better deal even in terms of cost, or effective interest rate paid. Even for graduate students, IDEA can still be a better overall deal, especially for borrowing during the graduate years.

A third major potential advantage of IDEA is that it solves the middle income access problem we've all heard about. We all know that it would cost a lot of money to open up eligibility for Stafford loans to all students regardless of family income. But when you turn things around and look at the problem from the IDEA perspective, the whole picture can change. If the version of IDEA enacted charges extremely high income graduates a limited amount of premium interest, you would actually want students from higher income families to participate because they tend to have higher later incomes themselves and some of them would make some limited premium interest payments helping to subsidize low income borrowers.

A fourth major advantage of IDEA is that it rationalizes and dramatically simplifies the whole question of deferments and forgiveness provisions that, under the current system, constitute an arbitrary, unfair, complex mess that's next to impossible to keep track of. Under IDEA, everyone who needs a deferment because of temporarily low income, or forgiveness because of permanently low income, automatically gets it, with no fuss and no extra record keeping. And we in the Congress don't have to argue about which occupations are more or less deserving.

A fifth IDEA advantage is that it solves the problem of what to do about the severely troubled HEAL program for medical professions students. Whether or not HEAL is repealed IDEA should largely drive HEAL out of business because it is much more attractive for those students, who typically face extreme problems of immense loan repayment burdens and insufficient income shortly after leaving school.

The final IDEA advantage I'd like to mention is that this approach should save immense amounts of money, between $1 billion and $2.7 billion per year, depending on the approach adopted. That is a crucial point. If we want to spend more money on Pell grants or other parts of the Higher Education Act, we've got to find savings somewhere, and IDEA is a perfect source because it saves these tremendous amounts while still providing a much better loan program than the ones we've got now.

You might well ask at this point how this is possible. How can we save money while providing a fairer and better deal for students, solving the HEAL and middle income access problems, and providing universal deferment and forgiveness according to need? The answer is that there are four major sources of efficiency in IDEA that correspond to four sources of waste in Stafford and other current loan programs.

The first of these is that IDEA practically eliminates defaults, which are probably the biggest source of waste and potentially the biggest source of savings in the current guaranteed student loan programs. Under IDEA, there is no reason to default because repayment is based on ability to pay and is capped at a reasonable percentage of income. And there is no opportunity to default because the repayment is part of one's income taxes. This alone is a potential source of savings on the order of a billion dollars plus.

Note that these savings have nothing to do with direct lending and everything to do with income-dependence—including the IRS collection, the ability to move peoples payments up or down flexibly over time, and the potential of receiving premium interest from high income graduates.

As you know, there is a direct lending proposal in the House reauthorization bill, but it is not income dependent and will not achieve any savings in default costs.

Even if IDEA is enacted only as a supplementary program, which doesn't repeal Stafford or HEAL, you can still reap large savings in the default costs of such loans by requiring that all new Stafford and HEAL loan agreements will carry a stipulation that if those loans go into default, they will be converted automatically into IDEA loans and become subject to IRS collection under the IDEA terms. In that way, IDEA will reduce default costs even under the programs which might coexist with it.

A second source of efficiency in IDEA is precise targeting of subsidies. IDEA provides subsidies to all those who need them, only to those who need them, and to the extent of their need. In a sense, borrowers who might have defaulted under programs like Stafford have what would have been their defaults defined out of existence under IDEA. But, later on, if their income goes up, they come back into repayment easily under IDEA, so that the government doesn't spend more on subsidies than people need.

An income dependent program offers the opportunity to pay for those subsidies, at least partly, from limited premium interest payments from high income graduates—that is, from those whose investments in education have paid off most handsomely. That's exactly the reverse of the Stafford program, which, on average, subsidizes high income graduates in preference to low income borrowers, who have low incomes in many cases precisely because they didn't graduate or invested only in shorter term programs.

This is not an essential feature of an income dependent program, and the Simon-Durenberger proposal does not include it. But I would note again that it does help justify opening the program to everyone regardless of family income.

The third major source of efficiency is a lower cost of capital. Whereas existing programs use private capital at politically negotiated interest rates, IDEA uses government capital at a much lower cost. That's another billion dollar potential source of savings at no cost to students. While it may appear that this source can be tapped with a non-income dependent direct loan approach, such as the Andrews approach in the House reauthorization bill, those proposals suffer from potential collection problems. Only the IDEA-type approach justifies collection as income taxes by the IRS, which solves the collection problems associated with direct government loans.

Moreover, in any direct lending proposal you must consider administrative costs which may partially or wholly offset savings in cost of capital. After all, in the Stafford and other guaranteed loan programs we're not paying banks only for the use of money. We are also paying for a certain amount of administration. If you just move the same type of administration somewhere else, it will cost the same amount of money. IDEA, on the other hand, offers greatly simplified administration, which is its fourth source of efficiency. Under IDEA, loan origination is simple because there are no extra institutions involved and because there is no needs analysis. Anyone attending an approved school is eligible regardless of family income. Practically all the schools have to do (besides providing information on the program) is compile lists of applicants and send them off to the Treasury.

Loan collection is also as simple as it can be—schools would have no role at all other than reminding departing students to begin withholding IDEA taxes. And since the IRS is already in the tax collection business, and repayment is included as personal income tax liability, the added costs to the program would be small. No additional tax returns are generated, as those who fall below the filing threshold, and therefore owe no regular income taxes, owe no IDEA payments either. In fact, IDEA should simplify the job of the IRS, because it will get the IRS out of the business of withholding the refunds of loan defaulters.

In short, the IDEA concept increases the availability of funding, reduces defaults, and makes repayment more manageable.

To the extent that subsidies are involved, they are progressive. And the money goes where it should go—to students who need it—rather than to bankers, defaulters, administrators, and the richest graduates.

In the process, IDEA frees up a great deal of federal money which can be used for education grants or for deficit reduction. The IDEA loan program provides an innovative and cost-effective way to ensure access to higher education for all students, and I encourage this committee to study the IDEA concept and to support it.

Senator SIMON. And then some of these points, like the cost of attendance, for example, as Senator Coats mentioned, we can work out. We're talking about a very, very limited entitlement, and it is voluntary for any school that wants to come in. My hope is that we can move in this direction. And while people attack entitlements, I can remember when a judicial nominee was up, and he read a speech where he attacked entitlements, and the Senator from Massachusetts said, "What entitlements would you like to get rid of?" and I didn't hear any entitlements anyone wanted to get rid of.

Senator COATS. Well, if I could just respond to that, sometimes the answer is not what entitlements you'd like to get rid of, but do we want to add more given our current national debt and given our current budget problems.

Senator SIMON. I promised the chairman I would make this brief. This is the first entitlement you've ever heard of that will save money, and it will.

Senator COATS. That's not the first time that statement has been made.

The CHAIRMAN. Senator Durenberger.

Senator DURENBERGER. Mr. Chairman, the important point for me this morning is, I think, to compliment my colleagues because we are still here an hour and a half later. I think it is the quality of the questions that is going to help the quality of the statements that come behind us, and the real experts, and I compliment all of you for your questions and your comments.

On Dan Coats' point, once we head down this course, we're going to head down this course. We aren't playing games. Once we head this way, we're heading this way, and if you are hesitant about it, then it is really appropriate to ask these questions.

But with regard to the point you made about dealing with the cost of higher education, that's the one thing that bothers me the most about this proposal, and I have said this here before. But we aren't going to find the answer to how to restrain the cost of higher education before we have to deal with the issue of access, and that's our quandary.

At least we're dealing with the issue of access differently from what our predecessors did in 1965. They had an access problem for the poor and the elderly to health in this country. They fixed it with an entitlement and sent the bill to the grandchildren. That's the problem.

This one doesn't send the bill to anybody other than those who are the potential beneficiaries of that education, and they are the ones who will have to be responsible for making the judgments about how much of what do I want, and will I work to get something out of this program, because it's going to cost me—not somebody else—to pay it back.

I think as you labor with entitlements and giveaways and all the rest of the things I hear particularly from others not here today, that's the big difference between this kind of an approach and the ones that our predecessors did in health care in 1969.

The CHAIRMAN. Thank you very much. We are really grateful to all of you.

We now welcome our second panel. John Silber is president of Boston University; William Byron, president of Catholic University; Phyllis Hooyman, the director of financial aid at Hope College in Holland, MI; and Barry Bluestone, professor of political economy at the University of Massachusetts in Boston.

I want to welcome my fellow citizens from Massachusetts who have thought about this issue in great deal and want to recognize in particular the extraordinary leadership that President Silber has had in this area. This has been an issue he has thought through over a long period of time.

Just of interest to members of the committee, I was looking back through the history of the Elementary and Secondary Education Act and the early debates in the Sixties, and old Ralph Yarborough included a study of John Silber's about the importance of early education. We are beginning to come around to the acceptance of that reality as well.

So we are grateful to all of our panelists who have given a good deal of thought to education issues in general and in particular to the matter that is before us.

I might ask President Silber if he'd be good enough to start off.

STATEMENTS OF JOHN SILBER, PRESIDENT, BOSTON UNIVERSITY, BOSTON, MA; FATHER WILLIAM J. BYRON, PRESIDENT, CATHOLIC UNIVERSITY OF AMERICA, WASHINGTON, DC; PHYLLIS K. HOOYMAN, DIRECTOR OF FINANCIAL AID, HOPE COLLEGE, HOLLAND, MI; AND BARRY BLUESTONE, PROFESSOR OF POLITICAL ECONOMY, UNIVERSITY OF MASSACHUSETTS, BOSTON, MA

Mr. SILBER. Senator Durenberger ended his testimony by quoting from an address that was made by Senator Kennedy back in the Seventies when he introduced the legislation to establish a program very similar to the one that is before you today. It was a self-reliance loan program called "the tuition advance fund," but incorporating many of the ideas that are in here today.

The reason I think Senator Kassebaum and others were cosponsors there is because it was a somewhat different program than the model that is before you this morning. It was a program that was designed to really solve the problem of access to higher education, and I suppose its boldness and its comprehensiveness made it seem unrealistically expensive for enactment. And consequently, after all this lapse of time of 12 years, in which Senator Kennedy has continued to be concerned with this, and Senator Simon has become a Senator and continues to be concerned with this, and many others have worked on it for so many years, they have now decided on a pilot program.

A pilot program if it is going to work has got to offer a complete conceptual unity. Suppose we had a pilot program for high speed railroad traffic for the United States, and we decided to do it between New York and Washington. It would be essential to lay rails and to have the cars and the engines to make it possible. Suppose you had a pilot program of this sort, but you left the wheels off the left side of the vehicles, or you left some of the track off, or you didn't build some of the bridges. You'd have a disaster on your hands.

Now, what I would suggest to the committee is let's have a pilot program of a self-reliance loan, but make it a pilot program out of that bill that Senator Kennedy presented back in the late Seventies, which was a comprehensive approach that made sense, that had all pieces fitting together, so that it would actually work—and, if you find the cost too much, then reduce the size.

If you were to have that program as a pilot at $1 billion a year, increasing to $2 billion the second year and $3 billion the third and $4 billion the fourth, it would be fully phased in at $4 billion, and within 10 years, you would see that the repayments, always increasing every, single year, would begin to achieve the objectives that he had in mind, which was a self-sustained national endowment for the financing of higher education that ultimately would impose no cost on the taxpayer, but leave every individual student with the obligation of assuming the cost of the education he received, recognizing that education is an investment, not a matter of consumption, and that the individual who has been educated, and therefore has an annual income substantially higher than one who has not been educated will be so benefited that he can easily afford to pay the cost. And it also had an element of justice built right into it. Who should pay the cost of one's enhanced capabilities as a result of education if it is not the person who is the beneficiary?

This placed the responsibility for paying on the individual, and it gave the opportunity for education to everyone. That system made a great deal of sense. And if you ask where are we going to find the $1 billion rising to $4 billion, try one penny on the gas tax the first year, two pennies the second year, three pennies the third, and four pennies the fourth. Ask Mr. and Mrs. America, "Would you pay an extra penny for a gallon of gas if your child had the ability to borrow enough money on this kind of system to be able to finance his college education?" and the answer would be a resounding yes, and the middle class would say, "My God, the Congress has awakened, and they care about the middle class and are doing something for them."

At the present time there is no question that the Pell Grants, the Stafford loans, the Perkins programs give educational opportunity to the poor, and we don't need to worry about the rich. But the middle class is in a terrible jam. When I testified on this subject before, Senator Durenberger raised objections with me that he said he hoped I would think about and get back to him on. One of the objections was that under a program of self-reliant loans where the individual who receives the educational benefit is the one who must pay for it, he asked aren't we transferring to the kids a burden that should be borne by the parents.

Well, we ought to ask the question: How did the parents do it? The fact is that, except in the families of the very well-to-do, the parents never did it. It was kids who worked their way through college at a time when it was financially possible to do so, or they received an entitlement called the GI bill, which made money for this country and made money for everyone person who participated in it. Or they got a scholarship. But the parents never paid for it.

When my mother completed her education, she did it by going to night school and to summer school while she was a full-tine teacher. That's how my parents got their education; they paid for it themselves. And when it came my turn, they helped me as much as they could, but it wasn't remotely enough, and I like most of the people in my generation paid our way through college by a bunch of odd jobs.

I did it, as the Senator may imagine, by being a debate coach. I cashed in on my argumentative nature. [Laughter.]

The gimmicks people have used have indicated the extent to which education is a do-it-yourself project. But we have seen in the last 10 years that the cost of education has simply gone beyond the ability of young people to earn enough to pay for it.

We had this last year at Boston University to raise our budget for student financial aid by $15 million, and next year we'll raise it by another $12 million. Each year it has had to go up because we had a 22-percent increase in the number of students who qualified for financial aid, and there simply isn't the money out there.

We are going to have to do something about this if we want an educated Nation.

Now, when we come to the question of controlling costs in the schools, this year Boston University raised its costs by 2.9 percent for next yeai That's well below the level of inflation. And why did we do it? Not because we liked to cut back that hard on our budget, particularly when we have to find another $12 million for student financial aid. We did it because the competition requires it. The State institutions are out there, heavily subsidized by the taxpayer; that put a definite threshold on the ability of independent universities to raise their tuition.

Now, when we talk about the advantages of this loan program, and one speculates about whether it will save money or reduce red tape, there is really no question about that. If we introduce a program that recognizes that education is an investment and that persons who are educated earn more and make the country more prosperous and contribute to economic competitiveness all over the world, then we recognize that it is folly to have a means test for eligibility to be educated. It is as foolish as to require an IRS form in order to get on the turnpike. The program should be available to anyone, and you ought to design it such that people who are so financially well-off as not to need it will not use it.

In Mr. Kennedy's original bill, he had a 50-percent surcharge added immediately on to the amount of money that was lent. When the person borrowed, he understood that he paid back 150 percent of what he borrowed. If he was going to be well-off and be able to pay back rapidly, he knew perfectly well that the effective interest rate would be around 12–15 percent, and it would be a good deal. So this discouraged participation by those who did not need it. At the same time, it relieved the universities of means tests. Means tests are the biggest item of red tape in student financial aid that there is. It takes an enormous amount of time.

And I can assure Senator Kassebaum that this program will greatly reduce red tape on the part of the university and the bureaucratic costs that go with it. If the Department of Education doesn't know how to handle this, then they can sublet this as a contract to Boston University, and we'll show them how to run it. There are any number of institutions that can run this.

And I can't believe for one moment that the IRS doesn't know how to collect it. They do very well collecting from me and most of my friends, and I daresay they will collect from the students who borrow under the program. Obviously, they would have to have a new box on the W–2 form. That won't cost very much to introduce. And if a person checks that box that he has indeed received a self-reliance loan, then the employer presumably will automatically deduct as a part of payroll deduction a percentage appropriate to the income that person is earning. This greatly simplifies the process of collection.

This should be understood as an advance of taxes, so that there is no possibility of default. Remove the possibility of bankruptcy. No eligibility for bankruptcy because this is an advance against taxes, and it is returned by taxes. Under this system, there are only three normal means for avoiding repayment. One is death, another is disability, and the third is Leavenworth, and none of those are particularly attractive alternatives to the payment of one's debt.

In this way we can be sure that we will save the $3 billion currently being spent in default of these loans at the present time.

The self-reliance scholarship makes a great deal of sense. What I would suggest is to introduce it as a very limited pilot program of Senator Kennedy's original bill. That will work. It will amortize itself. It will show you the possibility of establishing a permanent national endowment, self-sustaining, for the financing of higher education.

In the present form, however, with the greatest respect for my friend, Senator Simon, I don't believe your charts. As I have been able to look at it, I don't know how they were calculating the T–bill rate, but the current T–bill rate is a very lovely 4.5 percent; add 2 percent to that, and you've got 6.5 percent. That is almost a historical low in modern times. The average for the 1970's was 6.3 percent, which would give one, when you add 2 percent to it, 8.3 percent.

The average in the 1980's for the 52-week T–bill was 8.9 percent. Add 2 percent, and you have 10.9 percent. Suppose we take an average over that 20 years. It is 7.6 percent for the 52-week T–bill. Add 2 percentage points, and we have a 9.6-percent interest rate.

Let's suppose a student uses the $25,000, and if he has any financial need at all he will need every penny of that. By the time he graduates and starts to repay, he owes $33,191 if that average obtains, and the interest is over $3,000. If he has a salary of $20,000, he will have a shortfall of almost $1,800 a year.

If, 5 years later, he does very well, and he now has a salary of $30,000, he will have a shortfall of about $1,000. If, in the next 5 years, he reaches $40,000, which is doing extremely well, he will have a shortfall of about $400.

So over that 10-year period, doing extremely well from graduation to the time he's out 10 years, he will have had a negative amortization of about $1,000 a year, so that when you compound that interest, he will owe at age graduation plus ten, $47,591. And if he wants to be able to hold it at that level and not have any further negative amortization, he'd better have a sudden salary increase to $68,000, and if he expects to pay it off in the next 15 years that remain, he's got to have a salary of $85,000.

Now, you can shift these numbers some by supposing that instead of the average being 9.6, that maybe it is only 8.6 or 7.6, but as you reduce that average, you reduce the credibility of the projection.

The difficulty with this is that this bill as it now stands also removes the in-school subsidy on interest rates, which is 3.25 percent plus the T-bill rate. That offers a student who has a financial need a better deal than this deal. And the middle class is not going to rise and cheer with the passage of this bill as it presently stands because they will see this as a disadvantage. If they have eligibility for the Stafford loan, they will take the Stafford loan any time, with that subsidy of interest, over this new formula.

On the other hand, if you were to introduce, let's say, in five or ten independent colleges and universities and five or ten State colleges and universities the tuition advance fund plan as originally proposed by Senator Kennedy, you would then have a manageable program that could demonstrate the soundness of this system for the financing of higher education. Those students who participated would not be eligible for any other Federal programs; they would simply finance the cost of their education through that means. And in trying out that pilot, I think we would demonstrate the soundness of it.

I think that demonstration has been made with theoretical soundness such that we ought to introduce it as a total piece of legislation for everybody, substituting this for the existing student aid programs and making it a universal program of universal access but universal responsibility on the part of those who are beneficiaries.

But if in this climate it is not possible to go all the way, then I would suggestion going as far as we can with a conceptually sound pilot program. But I call your attention to the deficiencies in the pilot as it is now designed, because you took one wing and half the stabilizer off Senator Kennedy's plane, and I think he would be very disappointed if it tried to fly it. I don't want to see him killed in the crash that would result from this, nor any other member of the Senate, because your heart is in the right place; you are thinking this thing through, and you are trying now to do something for middle class children and their parents so they can be educated, but you need a conceptually sound vehicle in order to do so.

There is no question, as my colleague from Hope College will tell you, that universities can easily manage the kind of program Senator Kennedy proposed originally or the program that is before us right now. And schools that aren't smart enough to figure out how to do that don't need to apply.

So we shouldn't waste much time with objections of that sort, it seems to me. And we should not be frightened by the bugaboo of entitlement, because if this country is entitled to a future, it must educate its young people. If we fail to educate our young people—and we will fail if we don't entitle them to access to college and universities so that they can complete this higher education—we will lose our entitlement to a future.

The CHAIRMAN. Thank you very much.

Father Byron.

Father BRYON. Thank you, Mr. Chairman. Forty-five years ago I was sitting in college on the GI bill, and reflection on that experience has really brought me to a point of commitment to this point of direct lending, and that is why I am here today.

I am now president of the Catholic University of America, and I have been in higher education administration for over 20 years, and I have seen my generation in function of the benefits they received from the GI bill move on to positions of responsibility, positions of influence, and return to Treasury far, far more than was ever laid out in support of their education.

I think if we all came to the table with a blank piece of paper and said we were going to redesign the higher education student assistance programs, we'd have something far different than what we have today. And I think a central element of the new design would be this income-contingent payback program that we're talking about today. It seems to me that all we have to do is take the classic, conservative principle of working your way through college and reverse the sequence—go to college first and work your way through later on.

There is going to be resistance to this proposal, of course. We have already heard some of it this morning. Sadly, I think there is going to be some resistance within the higher education community. The specter of complicated administration—I agree with what President Silver said—if it's too complicated to run, let them sit out. But we also right now at this moment are running a Perkins loan program based on campus, and we've got a mechanism where it can be done.

I would like to see a larger demonstration project, but I'm not all that confident it's going to be easy to enlist participants because there is a lot of unease. There is unease about IRS involvement; even though IRS is involved with the taxpayer, it is only peripherally involved with the institution.

All of this presumes the willingness of a really broad spectrum of participating colleges and universities, and I for one am willing to do some of the missionary work to try to get people onboard. But I applaud the initiative. It's a delight to see that the acoustics have improved here on Capitol Hill for this idea of income-contingent payback, far different from when John Silber was talking about it back in the Seventies.

I'd just like to make one closing comment and put my statement in the record. The comment is this, that on entitlements, it is possible—you might just think of this small adjustment. The SLS is now an entitlement. Perhaps anybody who comes into this program could trade off participation in this program for the entitlement privileges of SLS. That may be one small way of holding the balance in the context of this demonstration.

I'll put my statement in the record, Mr. Chairman, and we can get on to hear from Barry and get into some questions.

Thank you.

The CHAIRMAN. Thank you.

[The prepared statement of Father Byron follows:]

PREPARED STATEMENT OF FATHER BYRON

Mr. Chairman and Members of the Committee, I welcome the opportunity to present my views on the need for design modifications in our present system of student aid.

If every college president in the United States and every member of Congress could bring an open mind and a blank sheet of paper to the drawing board, a new design would surely emerge for federal financial assistance to college students.

We all know the problem. The prospect of unmanageable debt is discouraging some young people from beginning college. Mounting indebtedness is frightening those already there. It forces some students out of the higher-priced independent colleges into the public sector, or, from either sector, out of higher education altogether. And for those who stay, the burden of debt complicates life unnecessarily in their young adulthood. It tilts their career choices toward higher anticipated income streams and away from undercompensated human service employment. The debt burden also weighs-in heavily and negatively on the financial foundations of many new marriages. The situation needs attention. Hence the need for a clean sheet of paper and many open and creative minds to come up with a new design for federal financial aid.

I think we should take another look at the "working-your-way-through-college" principle, and think about reversing the sequence. College first, then "work your way through" by permitting the Internal Revenue Service (IRS) to withhold a fixed percentage of the post-graduation paycheck until there has been repayment with interest of the federal funds advanced to cover the costs of education. Repayment would be income-contingent. This makes the obligation manageable and, since repayments would be extracted from gross income by IRS, this obligation moves to the front of the line ahead of all other personal debt responsibilities.

A federally-capitalized revolving fund would provide the wherewithal to meet college expenses. There would be no "defaults," because IRS would be in the picture and tax evasion, an unattractive and high-risk option, would be the only other way out. Repayments during a graduate's working lifetime would replenish the fund and thus make the same form of financial aid available to subsequent generations of students. Once up and running, the revolving fund would have "perpetual motion" and the student-aid dilemma would be solved.

This is what the public policy vocabulary calls a "direct lending" plan. The version I favor includes IRS as a collection device with appropriate phase-in provisions, this approach could eventually replace Stafford loans and some other present forms of Federal student aid.

Resistance to this proposal can be expected from several quarters. College administrators are wary of excessive governmental intrusion. IRS involvement, even though it would be with the student and only peripherally with this institution, is resisted. Some administrators in the lower-priced, state-subsidized, public sector of higher education will oppose the plan. It gives all students a realistic choice by putting private higher education within their economic reach.

The banks will resist. They like the Guaranteed Student Loan (GSL) program (now known as Stafford loans) even though, depending on the arithmetic of a particular year, it costs the Federal treasury between 35 and 50 cents on every commercial bank dollar loaned. The secondary marketers of GSL's want no change, nor do the various loan-servicing agencies. Their business would be reduced or eliminated if direct lending of Federal dollars to enrolled students through the institution where they enroll were to replace our present system.

Some legislators who have labored long and hard not only to construct our present complicated system of Federal student aid, but also to keep it in place, will be understandably reluctant to dismantle it, or even tinker with it, for an unproven alternative. Others are ready to exercise both vision and care in changing the present system.

There is an intellectual appeal, a compelling logic, that suggests the direct-lending design is the way to go. The blank sheet awaits policy architects capable of designing a student financial assistance program that is characterized by universal eligibility, direct lending, income-contingency, simplicity, workable terms, and phase-in choices that would retain present programs as viable options. We need a direct-loan demonstrationproject large enough to produce a valid test of this idea on its merits.

All of this presumes the willingness of a broad spectrum of participating colleges and universities whose presence in the demonstration project will require both vision and courage now, and will serve in years to come as a badge of honor for having led higher education's tuition-dependent institutions out of their present economic insecurity toward financial stability. It can happen. There can be genuine access and meaningful choice for any student capable of benefiting from the rich developmental opportunities colleges can offer.

Institutions of higher education must not be scared off by those who raise the specter of government regulation and administrative complexity. The direct-lending idea is, as Norman Corwin remarked many years ago when speaking about brotherhood, "not so wild a dream as those who profit by postponing it pretend."

Mr. Chairman, I published a book in 1989 called *Quadrangle Considerations* (Chicago: Loyola University Press, 333 pp.). Chapter 25, "Paying for College" makes the case for the income-contingent payback proposal in greater detail. I submit a copy of that chapter for the record. Thank you.

The CHAIRMAN. Thank you.

Ms. Hooyman.

Ms. HOOYMAN. Mr. Chairman, members of the committee, my name is Phyllis Hooyman, and I would like to request that my full statement be entered into the record.

I am director of financial aid at Hope College in Holland, MI. We are a 4-year liberal arts college, enrolling approximately 2,800 students. Under the current Stafford loan program, formerly the Guaranteed Student Loan program, my office has processed loans for 1,100 Hope students this year, totalling $2,805,000.

I have worked in financial aid for 14 years. I am a past president of the Michigan Financial Aid Association, and I currently serve as chair for both the MSFAA and the Midwest Association of Student Financial Aid Administrators Federal Issues Committee.

I appreciate this opportunity to testify on the income-dependent education assistance or self-reliance loan program contained in S. 1150, the revised version of which is a creative response to the need for increased grants and loans within the constraints of the current budget provisions. My colleagues join me in congratulating you on this landmark piece of legislation which has indeed brought financial aid once again within the reach of middle class families. We hope that appropriations in the future will bring this aid within their grasp.

As it exists, the GSL program is often a bureaucratic, time-consuming and frustrating process for students, parents, institutions and financial aid officers. A student borrowing under this program may eventually be involved with as many as six different agencies during the life of the loan—the school, the lender, the guarantor, a servicing company, a secondary market, and the Federal Government—each with its own application, its own deadlines, it own set of regulations and its own policies.

Echoing what Father Byron said earlier, if given the luxury of drafting the ideal Federal direct lending program from scratch, my student aid colleagues and I would attempt to create a program that adhere to the following general principles.

First and foremost, a direct loan program must convert the savings into increased financial assistance for students. A direct loan program must be financed through direct Federal borrowing from the private sector by the Secretary of the Treasury. A direct loan program must be an entitlement, with no limit on the amount of capital available to finance loans for qualified students and their parents. Capital availability must only be determined by borrower demand and eligibility, as is the case currently under the GSL program.

A direct loan program must be simple. A direct loan program must restore integrity to the student loan process. Finally, a direct loan program must make repayment of student loans a direct and straightforward process. And I see three ways that this could possibly be accomplished.

First, through competitive private sector contracts with features to enhance performance. The Secretary of Treasury could service loans to the Internal Revenue Service or private sector servicing could be combined with existing IRS withholding options, thereby allowing borrowers to authorize employers to withhold and forward payments to designated servicers.

If structured according to these principles, there is no need to set up a pilot or demonstration direct loan program. Based on the above principles, direct lending is not an innovation but the application of successful components of past student aid programs. Direct financing for student loans worked in the past as an effective means of securing capital for Sallie Mae until 1981. Direct origination of loans by schools has flourished under the Perkins loan program since 1958.

To implement direct loans successfully, the numbers of schools participating must be large enough to allow for Federal systems building. Currently more than 8,000 schools participate in the GSL program. To ensure a truly operational direct lending program, now just a research study, we must include a substantial percentage of these schools in he initial cohort. My ideal that I would put forward here today would be a minimum of 500 institutions.

In addition, the criteria by which participating schools are selected must be broad enough to include institutions of all sectors and sizes.

Finally, the initial cohort of participating schools must meet certain performance standards.

If structured according to the principles above, and implemented along these guidelines, a direct loan program could be easily administered by an institution such as Hope College. I would not have to hire additional staff to process direct loan. I have a full-time staff of six individuals, and I find that I could easily shift what I am currently spending in the bureaucracy of the Stafford loan program to process GSL applications in terms of time commitments, incoming GSL checks, etc. I could take that time to process direct loan promissory notes and reconcile student billing accounts. That would be easily accomplished.

In fact, the current Perkins loan program, which serves as a model for direct lending, is an easily administered and simply formatted Federal program which serves our students effectively and carries a far lower administrative burden on the GSL program.

For our students, and most importantly, direct loans would mean more timely crediting of funds to their accounts and a significant savings of costly guarantee and origination fees—not to mention a considerable savings of time and energy in the application process.

The self-reliance loans authorized under the income-dependent educational assistance program meet many of the benchmarks of an ideal direct loan program. I would, however, like to suggest several modifications.

The primary driving force behind the concept of direct lending is the recognition that the current GSL program needs to be restructured. Although I would prefer to see full replacement of the GSL program with direct lending, I understand that any proposed change carries the possibility and risk of disrupting dollars available to students. Thus I also understand your decision to contain direct lending to a new supplemental program under Part B.

However, the source of concern can be addressed by replacing the current supplemental loan for students, or the SLS program, with self-reliance loans for participating institutions. In doing so, you will accomplish three significant goals.

First, you will begin to address the problems I just cited within the Guaranteed Student Loan program; second, you will avoid the need to create a new entitlement program; third, you will enhance the ability to evaluate direct lending by creating parallel programs under SLS.

You have clearly demonstrated that your primary reauthorization goal is to better target limited Federal financial dollars to students. For this reason, I urge you to create not a new program, but rather a new solution to the problems in the existing program. A thoughtfully constructed direct loan program that operates parallel to the current GSL system, rather than a pilot or demonstration program, will begin to achieve this goal for the largest number of students and in the least amount of time.

I thank you for this opportunity to testify before you and to make these comments, and I would be glad to respond to any questions you might have or provide further comment at a later time.

Thank you very much.

[The prepared statement of Ms. Hooyman follows:]

PREPARED STATEMENT OF MS. HOOYMAN

Mr. Chairman, members of the committee, my name is Phyllis Hooyman. I am Director of Financial Aid at Hope College in Holland, Michigan, a 4-year liberal arts college enrolling approximately 2,800 students. Under the current Stafford Loan Program, formerly the Guaranteed Student Loan (GSL) program, my office has processed loans for 1,100 Hope undergraduates so far this academic year, totaling $2,805,000.

I have worked within the financial aid profession for 14 years, am a past president of the Michigan Student Financial Aid Association (MSFAA), and currently serve as chair for both the MSFAA Legislative Committee and the Midwest Association of Student Financial Aid Administrators' Federal Issues Committee.

I appreciate this opportunity to testify on the income dependent education assistance or "self-reliance" loan programs contained in S. 1150, the revised version of which is a creative response to the need for increased grants and loans within the constraints of the current budget provisions. My colleagues join me in congratulating you on this landmark piece of legislation, which has indeed brought financial aid once again within the reach of middle-income families. We hope that appropriations in future years will bring this aid within their grasp.

As it exists, the GSL program is often a bureaucratic, time-consuming and frustrating process for students, parents, institutions, and financial aid officers. A student borrowing under this program may eventually be involved with as many as six different agencies during the life of the loan: the school, the lender, the guarantor, a servicing company, a secondary market and the federal government—each with its own applications, deadlines, regulations and policies.

If given the luxury of drafting the ideal federal direct lending program from scratch, my student aid colleagues and I would attempt to create a program that adhered to the following general principles:

DIRECT LENDING: BASIC PRINCIPLES

First and foremost, a direct loan program must convert the savings into increased financial assistance for students. The goal of direct lending is to increase federal student financial aid without increasing federal appropriations. The savings should be targeted to students in the form of increased eligibility for middle-income families, higher loan limits, elimination of fees, or increased grants.

A direct loan program must be financed through direct federal borrowing from the private sector by the Secretary of the Treasury. As described in greater detail in a recent article published by the National Association of College and University Business Officers (NACUBO), borrowing in this manner will allow direct federal lending to realize real and significant savings over guaranteed lending.

A direct loan program must be an entitlement, with no limit on the amount of capital available to finance loans for qualified students and their parents. Capital availability must only be determined by borrower demand and eligibility, as is the case under the current GSL program.

A direct loan program must be simple. It must reduce the generally acknowledged complexity of the GSL program by limiting the number of participating entities, reducing the number of transactions and the paperwork burden, and centralizing record-keeping.

A direct loan program must restore integrity to the student loan process. February 1991 Department of Education documents describe the GSL program as "error prone and extremely difficult to monitor and audit." These flaws can be minimized by consolidating financing under the Treasury Department, centralizing oversight under the Department of Education, and establishing clear, simple lines of accountability. Again, I refer you to the aforementioned NACUBO article for more details.

Finally, a direct loan program must make repayment of student loans a direct, straightforward process. There are three ways to accomplish this goal: The Secretary of Education could operate the servicing aspects of the program through competitive, private sector contracts with features to enhance performance. The Secretary of Treasury could service loans through the Internal Revenue Service. Or private sector servicing could be combined with existing IRS withholding options, thereby allowing borrowers to authorize employers to withhold and forward payments to designated servicers. A direct loan program also facilitates and eases loan repayment by providing better opportunities than the GSL system for implementation of creative features, such as income contingent and graduated repayments. This is possible because of the simplicity of a system with one source of capital and one entity responsible for servicing and collections.

If structured according to these principles, there is no need to set up a pilot or demonstration direct loan program. Based on the above principles, direct lending is not an innovation but the application of successful components of past student aid programs. Direct financing for student loans worked in the past as an effective means of securing capital for Sallie Mae until 1981. Direct origination of loans by schools has flourished under the Perkins Loan program since 1958.

IMPLEMENTING DIRECT LENDING

To implement direct loans successfully, the number of schools participating must be large enough to allow for federal systems building. Currently, more than 8,000 schools participate in the GSL program. To ensure a truly operational direct lending program, not just a research study, we must include a substantial percentage of these schools in the initial cohort. There should be no restrictions to limit the loan volume of a participating school or prohibit the participation of large volume schools. Rather, participation of large volume schools should be encouraged in order to achieve economies of scale.

In addition, the criteria by which participating schools are selected must be broad enough to include institutions of all sectors and sizes. The House reauthorization bill instructs the Secretary of Education to select schools which represent a cross-section of institutions of higher education in terms of size, geographic location, length of program, control and composition of student body.

Finally, the initial cohort of participating schools must meet certain performance standards. As in other new initiatives under the Department of Education, such as the quality control project, applicants should be required to meet performance standards which typically include recent successful participation in the majority of federal student financial aid programs, as measured by numbers of students, volume of dollars, and absence of significant liability in audits.

If structured according to the principles above and implemented along these guidelines, a direct loan program could be easily administered even by a small institution like Hope College. I would not have to hire additional staff to process direct loans—I could easily shift the administrative resources currently used to process GSL applications and incoming GSL checks to process direct loan promissory notes and reconcile student billing accounts. In fact, the current Perkins loan program, which serves as a model for direct lending, is an easily administered and simply formatted federal program which serves our students effectively and carries a far lower administrative burden than GSL's.

For our students, direct loans would mean more timely crediting of funds to their accounts and a significant savings of costly guarantee and origination fees—not to mention a considerable savings of time and energy in the application process.

INCOME DEPENDENT EDUCATIONAL ASSISTANCE

The self-reliance loans authorized under the income dependent educational assistance program meet many of the benchmarks of an ideal direct loan program. Eligible students enrolled at participating institutions are deemed to have a contractual right to receive a self-reliance loan once Congress designates the federal agency responsible for collecting these loans. Self-reliance loans direct benefits to students, with expanded eligibility for middle-income students and no origination or guarantee fees. Self-reliance loan ensure program integrity and simple lines of accountability.

However, some modifications to the legislation authorizing the income dependent educational assistance loans are necessary to ensure the success of self-reliance loans. I would like to address what I believe is the most significant modification.

The primary driving force behind the concept of direct lending is the recognition that the current GSL program needs to be restructured. There is considerable evidence that it is buckling under its own administrative weight. The largest insurer of loans, the Higher Education Assistance Foundation, is insolvent. Each percentage point rise in Treasury bill interest rates currently costs the federal government approximately $400 million in special allowance payments. Within the last year, the cost of burgeoning defaults passed the $3 billion mark. Authorizing a new program under Part D will not address these problems, but replacing the current guarantee program with a direct loan program will.

Although I would prefer to see full replacement of the GSL program with direct lending, I understand that any proposed change carries the possibility of disrupting dollars available to students. Thus I also understand your decision to contain direct lending to a new supplemental program under Part D. However, the source concern can be addressed by replacing the current Supplemental Loans for Students (SLS) with self-reliance loans for participating institutions. In doing so you will accomplish three significant goals. First, you will begin to address the problems I just cited with the GSL program. Second, you will avoid the need to create a new entitlement program. Third, you will enhance the ability to evaluate direct lending by creating parallel programs under SLS.

You have clearly demonstrated that your primary reauthorization goal is to better target limited federal financial aid dollars to students. For this reason, I urge you to create not a new program but rather a new solution to the problems in the existing program. A thoughtfully constructed direct loan program that operates parallel to the current GSL system—rather than a pilot or demonstration program—will begin to achieve this goal for the largest number of students in the least amount of time.

I thank you for the opportunity to make these comments and would be glad to respond to questions or provide further comment at a later date.

PORTFOLIO

The Direct Lending Debate

Making the Case for and Dispelling Myths About Direct Lending

by Thomas A. Butts and Elizabeth M. Hicks

Supporters believe direct lending would lead to substantial costs savings and improved service to students.

Direct lending is unquestionably the most hotly debated issue as Congress considers reauthorization of the Higher Education Act. If passed into law, the direct lending program would eliminate the role of lenders and secondary markets as middlemen in delivering student loans, a move that supporters believe would lead to substantial cost savings and improved service to students. It is an idea whose time has come.

Direct lending offers the best of both centralization and decentralization. Direct lending is a campus-based program which would eliminate the current system's confusing negotiations between the borrower and the college or university business office. Under direct lending, Treasury Department funds go directly into students' billing accounts without compromising standards of integrity and accountability. The participation of lenders and secondary markets would continue through loan servicing contracted by the Department of Education.

The benefits of direct federal loans to students hinge on the way the federal government accounts for credit it extends in the form of loan guarantees and direct borrowing. The government's move toward the use of direct rather than guaranteed loans, as signaled in the credit reform provisions of the Budget Reconciliation Act of 1990, makes the replacement of guaranteed student loans with direct loans a fiscally responsible decision.

Analyses conducted by the Department of Education, Congressional Budget Office (CBO), and Government Accounting Office (GAO) all state that a direct loan program with the same terms and conditions as the Guaranteed Student Loan (GSL) programs would result in savings of more than $1 billion, allowing for Education Department overhead and contracting costs. A direct loan program would save the government about 10 cents on every dollar loaned.

According to a December 1989 CBO study:

> The difference in the budgetary treatment between federal direct loans and guaranteed loans creates a bias in favor of guarantees because their costs are deferred. When the costs are known (after default) and finally recorded in the budget, they are well past the gov-

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ernment's control. Consequently, loan guarantees have been growing much faster than direct loans in recent years. The total cost to the government of the new guaranteed loans is now many times more than the cost of new direct loans.

Echoing the CBO report, the president's fiscal year 1992 budget stated:

> Clearly, credit reform is not 'just' an accounting change. It is an opportunity to see each program with fresh eyes. Credit reform asks the right questions: Who is being helped? By how much? At what cost. It focuses attention and budgetary decisions on the costs underlying each loan, juxtaposed with the borrowers who benefit from these programs. It provides perspective for both policy analysis and program management.

Similarly, the GAO stated in its 1991 report, *Student Loans: Direct Loans Could Save Money and Simplify Program Administration*:

> Before the Federal Credit Reform Act of 1990 (P.L. 101-508), the budget rules favored guaranteed loans over direct loans.... As a result of this accounting method, direct loans appeared much more expensive than guaranteed loans.
>
> Since credit reform, the budgeting rules allow a more equitable cost comparison of guaranteed and direct loans. Under the new rules, the budgetary costs of each program for a one-year loan cohort is the net present value of all costs associated with those loans. A guaranteed loan's cost is the discounted value of all interest subsidy and default costs, while a direct loan's cost is the initial outlay less the discounted stream of anticipated principal and interest repayments...
>
> A direct loan program operating in place of the Stafford loan program could save over $1 billion—present value terms—assuming the loans are made in fiscal year 1992....

AN ENTITLEMENT

Like Stafford Loans, federal direct loans would be funded as an entitlement under the mandatory part of the budget. As in the Stafford Loan system, no limit would be placed on the amount of capital available. Capital availability would be determined by student and parent eligibility and demand.

The House reauthorization bill (H.R. 3553) would provide entitlements for students and their parents, rather than guarantees to lenders, secondary markets, and guarantee agencies. Savings would be passed to students in the form of increased eligibility for middle-income students, higher loan limits, and the elimination of origination fees.

The direct loan program would be financed through the sale of securities by the federal government. This would be accomplished in the same way funding for the Student Loan Marketing Association (Sallie Mae) was provided until 1981. Under that procedure, the secretary of the Treasury Department, through the Federal Financing Bank, sold government securities to the private sector and made the funds available to Sallie Mae. That system worked well, and Sallie Mae is presently making payments on about $4.8 billion it still holds.

In the case of federal direct loans, the treasury secretary would make funds available to the secretary of education for allocation to institutions through the department's finance system from which institutions draw student aid funds. Institutions would be able to adjust their requests for funds according to actual student eligibility throughout the program year. Repayments would return to the federal government and would not accumulate in institutional revolving funds, as is the case with Perkins Loans.

According to the House bill, 500 institutions would be eligible to participate in the new program beginning July 1, 1994. An additional 1,000 institutions would be added for the 1995-96 academic year. In 1996-97 all eligible institutions would be able to participate.

Under H.R. 3553, the secretary of education would operate the servicing aspects of the program through competitive, private sector contracts, including a contract for management of the national direct loan data system and loan consolidation. Profit-making firms, nonprofit organizations, state entities, guarantee agencies, and institutions would be eligible to apply for service and collection contracts. Each college or university would be able to select a government contractor which its officials believe would best serve the institution and its students.

PROCESSING A DIRECT LOAN

An overview of how the direct loan process, as envisioned in the House reauthorization bill, would probably work is described below.

A student completes a federal financial aid application to apply for all forms of Title IV aid. The application is submitted to a processor, who in addition to computing a student's eligibility according to the federal need analysis, conducts central data base matches with entities such as Selective Service, the Immigration and Naturalization Service, the Department of Justice, and the National Student Loan data base.

The processor forwards its result, including default analysis, to the institution. The institution reviews the need analysis, determines the student's eligibility for all forms of Title IV aid, and sends the student an award notice.

The institution mails a standardized promissory note to eligible students. The promissory note includes only those data elements and identifiers essential to the disbursement of the loan, such as loan amount, student's name, student's permanent address, student's social security number, student's driver license number, name and address of student's nearest relative, name and address of other references, student's signature, and date. Because a significant amount of time may have elapsed since the National Student Loan data-base match, the student will certify on the promissory note that he or she is not in default on any Title IV loan or does not owe a refund for any Title IV grant or scholarship.

The student completes the promissory note, retains a copy, and returns the original to the institution. The deadline for submission of the promissory note could be the earlier of the last day of the award year, June 30, or the last date within the award year on which the student was enrolled and eligible.

The institution then reviews the promissory note to ensure that it is properly executed.

A growing alliance of college and university government relations and financial aid administrators is working with members of Congress, urging them to support a highly equitable and economically responsible system for expanding federal financial aid to students.

DELIVERING THE GOODS

No loan funds may be disbursed until the institution has received a properly executed promissory note. Loans may be credited to a student's account or disbursed directly to the borrower by check.

As under the Stafford Loan and Perkins Loan programs, the institution may advance federal direct loan funds by crediting an enrolled student's account no more than three weeks before the first day of classes. The institution may advance loan proceeds directly to an enrolled student no more than 10 days before the first day of classes. The institution must return any amount advanced to a borrower who officially or unofficially withdraws or is expelled before the first day of classes.

Loans disbursed directly to a student's account must be clearly identified as federal direct loan proceeds. Students are not required to sign an additional authorization or acknowledgment of receipt of funds at the time of disbursement.

At institutions using standard academic terms, the payment amount is calculated by dividing the total award by the number of payment periods.

Institutions not using standard terms must make at least two payments during the academic year, one at the beginning and one at the midpoint, after the student completes the hours for which payment was received. If the award is for less than an academic year, the total amount is divided by the number of payment periods the student will attend the institution.

If the student incurs varying educational costs and needs additional funds during a payment period, the institution may advance federal direct loan proceeds to the student to meet those uneven costs.

An institution may credit the loan proceeds to a new borrower's account before he or she receives an entrance interview. However, a new borrower must have an entrance loan interview within 60 days of the date the loan is credited to the account or prior to leaving the institution, whichever occurs first. An institution may not advance loan proceeds directly to a new borrower before he or she has an entrance loan interview.

Institutions can form consortia to administer the disbursement of funds and promissory note functions for them.

SMOOTH FLOW OF FUNDS

The institution draws down funds from the Department of Education Payment Management System. All regulations concerning the draw down of federal direct loan funds will be consistent with current procedures for campus-based and Pell Grant programs. At the beginning of each award year, an institution is given an initial allocation based on its previous federal direct loan volume. As the award year progresses, the institution's allocation is adjusted based on the actual number of eligible students.

An institution draws down funds and funds are posted to eligible student accounts within time frames consistent with existing procedures of the Department of Education Payment Management System.

The federal government makes money available as necessary to provide for prompt and continual flow of funds to eligible students.

KEEPING THINGS LEGAL

An institution is only required to report essential data elements to the department contractor, such as student's enrollment status; student's default history, if any; student's repayment history, if any; and student's annual indebtedness under the federal direct loan program. The secretary will, through his contracts with private sector servicers, offer a variety of ways for this data to be transmitted by institutions including modem, tape, floppy disk, or a cumulative paper roster. The institution should be able to elect the option. A separate form will not be needed for each loan applicant, such as the Stafford Loan application or Pell Grant Student Aid Report.

An institution will report any change in a student's enrollment status or loan eligibility to the servicing contractor. Any funds that are recovered from a student as the result of a refund or overaward are deducted from the next draw down of funds. The exact time frame for reporting the data to the servicing contractor will be determined by the education secretary, taking into account variances in institutional administrative capabilities. However, an institution should not be allowed to report less than quarterly to the servicing contractor.

As under the Perkins Loan program, an institution is liable for determining student eligibility, executing promissory notes, and disbursing funds to borrowers. However, unlike the Perkins Loan program, the institution is not liable for a loan during repayment if the promissory note was properly executed.

If the institution submits an improperly executed promissory note to the department contractor, the note will be returned to the institution promptly for correction. If the institution is unable to have the borrower execute a correct promissory note, the institution is liable for the loan only if the borrower fails to repay, as is the case under the Perkins Loan program.

JUMPING THE HURDLES

Several high hurdles must be cleared before direct lending is enacted, including a Senate package that does not yet include a direct lending provision and more bipartisan support in both the House and Senate than has currently been shown for the concept of direct lending. Senators Paul Simon (D-IL) and David Durenburger (R-MN) are pressing for a direct lending bill which features income-contingent repayments for students. The administration, which previously signaled the probability of a presidential veto of direct lending, now appears to be suggesting that the president may shift his views as part of the review of domestic policy issues. Although the Consumer Bankers Association, National Council of Higher Education Loan Programs, and Sallie Mae have come out against direct lending, a growing alliance of college and university government relations and financial aid administrators is working with members of Congress, urging them to support a highly equitable and economically responsible system for expanding federal financial aid to students.

Myths About Direct Lending

Direct Loans Increase the Federal Debt: Loan guarantees have the same effect on the economy as federal direct loans. Stafford Loan guarantees are listed in the president's FY 92 budget as a 100 percent contingent liability of the federal government—its responsibility for federal direct loans would be the same. Loan guarantees affect treasury bill rates virtually as much as direct borrowing, and loan guarantee programs are more costly overall. While raising capital for the $10 billion student loan programs wholesale through the sale of government securities to private markets adds to the $4 trillion dollar national debt, the lower cost of direct lending could reduce the deficit if the savings were not passed on to students. Loan guarantees are a part of the national debt but are not counted as such. Further, direct student loans are an asset of the government—an investment in its educated manpower which will be repaid.

Direct Loans Shift All Risk to the Federal Government: The guarantee program is structured to pass the majority of risk onto the federal government. States are not required to appropriate money for defaults, and the cost of risk borne by the guarantee agencies is covered by student insurance premiums. The only risk not assumed by the federal government is the risk to lenders when they do not perform due diligence properly. To argue that there is less risk to the government in the current program because lenders make errors is to

Myths About Direct Lending (Continued)

make the case that the program is poorly designed. The complexity of the program leaves many errors undetected. In contrast, direct loans reduce federal risk by providing clear, simple lines of accountability, government servicing contracts with positive performance bonuses, and direct government oversight to further reduce risk.

Direct Loans Would Increase Administrative Burden on Institutions: If a college, university, or trade school can process a Pell Grant or Stafford Loan, it can handle federal direct loans. For the student as well as the institution, the application process would work much like a combination of the Pell Grant and Perkins Loan programs. Students would sign promissory notes that the institution would forward to its servicing agent. The opportunity for error would be considerably less than with the complicated Stafford Loan program, and the simplicity of the operation would reduce overall institutional costs. Analyses conducted by institutional representatives indicate that the overall burden for administering federal direct loans is less than for the guarantee system.

If a college, university, or trade school can process a Pell Grant or Stafford Loan, it can handle federal direct loans.

Direct Loans Would Increase Institutional Liability: Institutions are currently liable for mistakes they make in performing their duties for all the student aid programs, including the Stafford Loan program. Because of the relative simplicity of the direct loan program, it would reduce institutional liability. Fewer chances for error would be present, and institutions would be better positioned to integrate management of direct loans with other Title IV programs.

Direct Loans Would Lead to Fraud and Abuse by Institutions: Fraud and abuse in the existing loan system are not confined to a few organizations. Without 45 guarantee agencies, 10,000 lenders, and 35 secondary markets to oversee, the department's efforts could be focused on contractors and institutions. Clear lines of accountability and financing managed by the Treasury Department, in conjunction with integrity provisions such as those in H.R. 3553, would reduce fraud and abuse in all student aid programs.

Direct Loans Would Give Trade Schools an Excuse to Raise Tuition: The administration has proposed increasing loan limits for the Stafford Loan program. If there is an incentive to increase tuition artificially, it would be the same with either program.

Phasing Out the Loan Guarantee System Would Be Difficult: Lenders would want their claims paid on outstanding loans and would, therefore, perform due diligence in loan collection as required by law. With about $50 billion in outstanding loans to be serviced and with a recent Department of Education study showing Stafford Loans to be more profitable than home mortgages and car loans, lenders would have economic incentives to remain in the program through the phase-in period. Guarantee agencies probably would receive an administrative allowance based on outstanding loan volume to assist in the phase-down process. As the failure of a major guarantee agency in 1990 demonstrated, loan guarantees can be transferred. H.R. 3553 has provisions to accommodate failed or weak agencies.

Ultimately, private lenders participate in the Stafford Loan program because it is profitable. In the transition from Stafford Loans to federal direct loans, one must assume the same economic process would continue. In addition, higher education does a far greater volume of other business with the lending industry than it does under the Stafford Loan program. During a transition, the banking community probably would be cooperative.

The Education Department Cannot Run the Program: With a July 1, 1994, start date for direct lending and a three-year phase-in plan, a smooth transition is possible. Federal direct loans are not guaranteed loans, and a comparison to guaranteed or other insured loan programs is inappropriate. Federal direct loans more closely resemble Perkins Loans. The secretary probably will make use of the best features of the Pell Grant and Perkins delivery systems for direct lending. The Department of Education has made significant progress with innovations to the Pell Grant program, including electronic processing and Stage Zero, which allows a student to use a computer to complete an application with immediate edits for errors. Electronic institutional applications for Perkins Loans and the recent electronic reapplication will save the department millions of dollars in printing, contract costs, and computing, while improving services to students. —•

The CHAIRMAN. Thank you very much.

Mr. Bluestone, we're glad to have you here again.

Mr. BLUESTONE. It is nice to be here again, Senator.

I'd like to thank Senator Kennedy and the committee for giving me this opportunity to testify on what I think is pathbreaking legislation. And while I have a complete statement that I'd like to see in the record, I will depart from that in order to raise issues that have not been raised here before, particularly some additional benefits of the program that I don't think my colleagues have raised.

Second, I'd like to respond to some of the criticisms that have been raised about the bill, and finally, deal with the issue that my colleague Mr. Silber raised about the financing of the program.

First of all, let's keep in mind that what we are talking about here is a program which has three very important elements: universality, direct Federal funding, and income contingency. It is really those three elements—and I like to refer to it as "UDIC" loans—universal, directly funded, income-contingent repayment systems—that make this particular piece of legislation so important, because each component of the legislation deals with a particular problem that higher education and postsecondary education in general now faces.

Second, I think what we should realize, and we could put a lot of numbers on it in terms of discrepancy between rising costs of education both in the private system, Boston University, and the University of Massachusetts at Boston where I teach, where our tuition and fees have doubled in the last 3 years as a result of cutbacks in State funding. And so what has happened is that many students who might have considered going to B.U. at that time and then considered to come to the University of Massachusetts and thought they could afford it are now finding themselves going to community college or not going on at all.

Solving that problem of the kind of "sticker shock" of tuition at the private schools and the problems that States are finding in financing their own education is something that this bill actually deals with directly.

There are also a number of benefits that I'd like to bring to your attention that we haven't talked about. Certainly, one of them is that under current loan programs, the repayments are essentially fixed, regardless of income. The problem with that is that while we continue to have discrimination in the labor market on the basis of race, ethnicity and gender, our loan programs don't reflect that. So it means that while women, for example, still only make about two-thirds of the typical male, a woman who takes the same amount of loan from one of the current programs must repay the same amount as a male who will on average make much more.

By making these programs income-contingent, we partially solve that problem by ability to make income a factor in the repayment.

The second factor—and I find this more and more important, both in the years I taught at Boston College, and now in my years at the University of Massachusetts—is that increasingly students are choosing what courses they go into on the basis of their ability to pay back their loans. As a result, we're not getting enough students choosing to go into primary and secondary education, or enough students going into other fields which perhaps pay less than lawyers and people who go to business school, but are critically needed in our society. And I think it is sad that under our current loan programs, students are making choices not on what they would like to do or what they could do for their country, but on the basis of whether they can pay back their loans.

Again, the IDEA program, as other UDIC programs, deals with that problem directly.

Let me deal with a few of the criticisms that have been raised by members of the committee here. One, of course, is that this is another program piled on top of an existing set. Indeed, one of the problems we have at our university, and I think it is probably true at Mr. Silber's university and others, is that there are such a morass of loan programs out there that in fact we spin our wheels, both families and students and administrators, in trying to figure out what package of programs we can put together to pay for our schooling.

This is an awful waste of energy. I would hope over time that if this type of program as envisioned in IDEA and self-reliance loans were to be successful as I think it will be, that we would streamline ultimately the system of postsecondary higher education finance.

Second, the whole question again of entitlement. We have to remember that these are self-financing entitlements, and as a result we are talking about an investment, not consumption. And if there is one thing we have to be very clear about in our country, it is that this is the time for investment, not consumption, and this bill is an investment bill, not a consumption bill.

When we talk about shifting decisionmaking to the Internal Revenue Service—a criticism raised by Senator Hatch—I can't help but think that despite the fact that we collect taxes through the IRS, and those dollars are used by our Department of Defense, I would hate to think that in fact it is the IRS that is running our defense policy. Indeed it is not. Under this system, despite the fact that IRS might be the agency that would collect the repayments, I doubt very much whether IRS would get its hands into the educational system itself any more than it controls our defense establishment.

I would also like to just emphasize a point that President Silber made, and that is in my experience the most difficult part of the red tape of our current programs is particularly the income and wealth verification. This is not only costly to the parents and to the students; it is the most costly, most time-intensive part of what our student aid administrators have to do.

By moving toward a universal program which is not needs-tested, which is not means-tested, we completely eliminate the income verification problem and therefore cut out most of the red tape for both the family and the institution.

And finally, the question of encouraging students to go into debt. There is a big difference, whether it be a family, a business, the Federal Government or a student, whether we are going into debt in order to forward our consumption or we are going into debt to forward our investment. And indeed what we need to do through this program is to make it very clear that going into debt for investment purposes is a good deal. And we know from every study that has been done in the last decade that one of the best investments anyone can make is not in the Dow Jones Industrial Average, it is certainly not in the General Motors Corporation today—it is an investment in higher education.

Finally let me deal just very quickly with an issue that, again, Dr. Silber has raised, and that is can we put together a set of repayment rates and a set of interest rates that would make this program ultimately self-financing.

I was only able to see this legislation literally yesterday, and so I have not been able to work through a simulation model for this particular program, but 2 years ago colleagues of mine at Boston College, Alan Clayton-Matthews and John Havens, and a colleague of mine at the University of Michigan, Howard Young, an actuary, put together a program called "Equity Investment in America." It had a slightly different refinancing system, but basically it was a UDIC, a universal, directly-funded, income-contingent program.

As part of developing that, we built a computerized simulation model at Boston College which could be used to test whether in fact this program would be fully self-financing. We did this for individuals, and we asked what would happen if a particular student at a particular age went out and borrowed, let's say, $20,000, $5,000 each year, toward their undergraduate education and then, based on projected incomes across the whole population—and we did that on the basis of Census data and relatively conservative estimates of what projected earnings growth would be—we came to the conclusion that if a student at age 21 left school, they would have to pay about 6.53 percent of their wages and salaries, not their adjusted gross income—wages and salaries is a smaller number—for up to 25 years in order for this program to be self-financing for the entire cohort of students who took those grants that year.

Now, this program is somewhat different but I would suggest that it would be a relatively simple problem to take the simulation models that exist at Boston College, perhaps other models that exist here at CBO and at GAO, and estimate precisely what interest rate we would have to charge and what the repayment rates would have to be to make this plan work.

Let me give you an example of where it could be much lower. We estimated what would happen if a particular individual who had lost his job decided to go back to school at a vocational training program which cost them just $2,500—how much would he have to pay over his future earnings in order to be able to pay that program back. The answer was 1.14 percent of wages and salary earnings.

So perhaps this idea of having 3, 5, and 7 percent could be enhanced and developed so that in fact we could make this work. I might add that based on our projections in terms of this particular individual who went back to school to learn computer programming, having lost his or her job, let's say, in the steel or the auto industry, would only pay 6 percent of his additional income over and above what he would have earned if he had not gone to school to pay for that vocational training.

I would contend that there is not a single investment in America that has such a high rate of return.

In sum, the program that you have put together here is something that is badly needed in America, and I think it is tugging at

America and particularly the middle class in very much the same way as the question of health insurance and ensuring that everyone has decent health care in this country.

As Senator Durenberger pointed out, there are many opinion polls that will tell you that families who are trying to deal with their health care problem, families who are trying to deal with the question of how to educate their sons and daughters, will tell you that this is every bit as important to them as what we do on health insurance.

So that I would hope that in this year, when we are really trying to win back the hearts and minds of Americas' middle class, you will strongly consider this as one way of doing it.

Thank you very much.

[The prepared statement of Mr. Bluestone follows:]

PREPARED STATEMENT OF MR. BLUESTONE

I would like to thank the Chairman and members of the Senate Labor and Human Resources Committee for the opportunity to testify on legislation that will provide for a national demonstration of an innovative program for financing higher education in America. The Income Dependent Education Assistance program, in my opinion, is an idea whose time has come. The "self-reliance" loans envisioned in this legislation will provide postsecondary students with a rational, equitable, and fiscally responsible method for financing their own educations.

This legislation exemplifies a fresh approach to one of the two domestic issues most on the minds of American voters as they look toward the 1992 elections. Unquestionably, the special Senate election held last November in Pennsylvania highlights the strong political sentiment in this country for innovative federal initiatives which can deal with the mounting problem of providing universal medical care. I am quite certain that if a opinion survey were taken today, the financing of postsecondary education would place high up on a list of politically salient issues along with the desirability of some form of national health insurance.

I would like to use this opportunity not so much to examine the details of the proposed loan program specifically under consideration during this hearing, but to testify to the need and propriety of the general approach to higher education finance found in the Income Dependent Education Assistance plan. In doing this, I will draw on my own work in this area—particularly in the background research for the "Equity Investment in America" program developed with the assistance of my colleagues, Alan Clayton-Matthews and John Havens of Boston College and Howard Young of the University of Michigan.[1]

ELEMENTS OF A GOOD POSTSECONDARY EDUCATION FINANCING SYSTEM

The Income Dependent Education Assistance (IDEA) Program contains three critical elements:

(1) ——Universal Eligibility

(2) Direct Federal Funding

(3) Income-Contingent Repayment

For brevity, we can refer to any higher education loan system containing these elements as a "U-D-I-C Loan Program".

The superiority of a UDIC loan program over current funding mechanisms for postsecondary education is based on a combination of all three elements:

Universal Eligibility—Under current financial arrangements, when it comes to paying for the costs of attending college, the wealthy and a small but select number of low-income students have things pretty well in hand. Healthier students, by virtue of their family's economic circumstances, generally pay these costs out of existing assets. High ability lowincome students, on the other hand, have available to

[1] See Barry Bluestone, Alan Clayton-Matthews, John Havens, and Howard Young, "Financing Opportunity for Post-Secondary Education in the U.S.: The Equity Investment in America Program," Briefing Paper, Economic Policy Institute, June 1990 and Barry Bluestone, Alan Clayton-Matthews, John Havens, and Howard Young, "Generational Alliance: Social Security as a Bank for Education and Training," *The American Prospect*, Summer 1990, pp. 15-29. Parts of this testimony are also drawn from a paper, "Income Contingent Student Loans," (October 25, 1991) which I co-authored with Jerome M. Comcowich of the University of Hawaii.

them an array of government and private sector grants and scholarships. In contrast, most low income and virtually all moderate income families have been left to fend for themselves. Just when postsecondary education is taking on greater value for the individual and for the competitive position of the nation, the current system of finance fails to provide a suitable method of finance for the vast "middle class."

The new proposed legislation deals with this issue directly. Under the IDEA demonstration program, virtually every student in a participating accredited institution of higher education would be eligible for loan support regardless of family income. Middle class students as well as those from wealthy families can take advantage of the proposed new program without placing any burden on the taxpayer since the full value of the loans plus interest is repaid. Current grant support is maintained for low income students in order to supplement available loans and provide an incentive for pursuing postsecondary education.

Direct Funding—Current federal loan programs (e.g. the Stafford and Perkins loans) provide an interest subsidy to students and a loan guarantee to private banks. The upshot of this system is an implicit subsidy to the banking system and a high rate of default. Defaults on student loans now run more than $1.5 billion per year.

By providing loans directly to students, bypassing the banking system, and by collecting loan repayments through a designated federal agency, direct funding reduces the administrative costs of the program and virtually eliminates nonpayment.

Income Contingency Repayment—Current loan programs require students to repay education loans at a fixed rate once they leave school. For many students this means they are forced to make repayments before their incomes reflect their added earning capacity. For others, this means repaying loans even if they are unemployed. This not only puts enormous economic pressure on students, but contributes to the high default rates found in current student loan programs.

Under the proposed legislation, loan repayments are income contingent. They vary with the income of the recipient and as such reduce the strain of repaying the loans, particularly under adverse economic conditions. As incomes rise, repayment increases. By setting repayment rates at a reasonable level and permitting borrowers to take up to 25 years to repay their loans, the government is effectively assured of a full return of principle and interest.

THE DISCREPANCY BETWEEN SCHOOL COST AND SCHOOL RESOURCES

The need for a new financing mechanism for postsecondary education is not difficult to document. At the very same time that schooling beyond high school is becoming more critical for individual as well as national economic growth, the cost of schooling is accelerating faster than the rate of inflation. Public resources available for loans and grants are by no means keeping pace with need. This is true for virtually all low income families and for the vast majority of the middle class. According to Kenneth C. Green of the Center for Scholarly Technology at the University of Southern California, the "sticker shock" of tuition and fees is forcing students to "buy down." Students who would have gone to private institutions are selecting public ones. Those who would have gone full time are forced to go part time. Some who would have selected 4-year colleges are going instead to 2-year schools, and more students from poor homes are going to vocational schools rather than college—if they go anywhere at all. A recent *USA Today* survey of high school graduates suggests that some students are now falling out, not just "buying down." One-third of the students in the survey intimated that they had delayed or indefinitely put off college because of the expense.

Anyone with college age children can attest to the burden of college costs. The College Board reports that by 1991-92 the cost to an in-state student for four years of school at a 4-year public college or university averaged over $25,000 including tuition and fees, room and board, and miscellaneous school expenses. The same education at a private 4-year institution was over $50,000. At the elite schools, total expenses run closer to $90,000. Yet, the amount of student aid available from the federal government in the form of grants and loans has not kept up with these costs. In 1979, according to the *The American Freshman* survey conducted by the Higher Education Research Institute at UCLA, nearly 32 percent of all freshman students received Pell grants to attend college. Ten years later, the percentage was down to less than 22 percent. Meanwhile the proportion of students receiving Stafford and Perkins loans from the federal government has risen only marginally, from 21 to 25 percent between 1979 and 1989.

The only reason why college enrollments have not fallen off precipitously in light of the growing gap between costs and aid is that colleges and universities are themselves assuming a greater share of the expense burden, providing more grants and scholarships generated out of their own revenue. The UCLA survey notes that between 1979 and 1989, the percentage of freshman receiving college grants and scholarships increased from 11.3 to 20.3 percent. Part of the higher tuitions being charged by schools is being used to subsidize students from low and lower-middle income backgrounds simply to maintain cultural and social class diversity in the classroom.

Part of the difficulty is that the federal government has moved to disenfranchise middle class students from federal assistance by restricting eligibility for grants. In 1979, the government set a $32,500 ceiling on family income for a student to be eligible for grant support. Today, despite inflation, a family must have an income no higher than $28,000 to be eligible for aid. Even then, if a student is still eligible for a grant, the amount provided has not kept up with increases in college costs. The largest of the federal loan programs, the Stafford Student Loan, provides a maximum of $2,625 per academic year for the first two years of undergraduate study and $4,000 for each subsequent year, up to a five year maximum of $17,250. Hence, a student who takes out the maximum amount of Stafford loans over four years still must come up with another $11,750 on average to attend a public university and at least $36,750 to go private. Perkins Loans have higher maximums, but fewer than 3 percent of all freshman take advantage of them.

For those not eligible for federal grants or loans, going to the private market can cost a bundle. One example is the Education Resources Institute TERI loan. With a TERI loan, a student can borrow up to $20,000 a year with no income limit or "needs test". However, the standard rate on TERI loans is the prime rate plus 2 percent. With a def erment on interest and principal while in school, a typical loan of this variety with a 5-year term carries an annual percentage rate (APR) of 15.3 percent at regular commercial banks. Professional Education Plan (PEP) loans for graduate study can be even more expensive if the student does not have a co-applicant. The APR on a 5-year loan with a 2-year deferral of principal and interest is currently in the range of 18 percent.

On top of high interest rates, the standard loan programs require students to begin paying back large sums as soon as they finish school despite the fact that their initial earnings are almost always modest. It is not surprising that the default rate on education loans is now 18 percent for those who went to 2-year public colleges, 14 percent for those who attended 2-year private schools, 7 percent for those who went to either private or public 4-year schools, and a whopping 33 percent for those who used their loans to go to trade schools.

THE PRACTICAL BENEFITS OF U-D-I-C BASED LOAN PROGRAMS

Restructuring post-secondary education finance along the lines of the proposed IDEA legislation deals directly with a number of problems inherent in current methods of supporting students in their quest for schooling.

(1) UDIC loans eliminate much of the morass of current federal loan programs in favor of one universal, comprehensive plan available to all postsecondary students.

(2) UDIC loans provide a substantially greater amount of funds under superior terms to most current programs, thus allowing students to better meet the rising cost of postsecondary education.

(3) UDIC loans are available to all students in accredited postsecondary schools regardless of family income. There is no "needs test". It is a middle class program every bit as much as one aimed at the low and moderate income student.

(4) Since repayment is based on actual earnings, there is effective deferral of principal and interest as long as the student is pursuing full-time studies and has little wage and salary income.

(5) Racial and gender discrimination in the labor market is not automatically ratified as is the current practice under fixed obligation loans. The income contingent feature of UDIC loans requires students to repay based on actual earnings and therefore takes full account of differences in earnings for any reason.

(6) Because UDIC loans are income contingent, students will be more likely to enroll in programs that conform to their academic strengths and career goals than in programs which simply hold out the promise of extraordinarily high earnings that can be used to repay fixed short-term loans. This may mean slightly fewer students opting for law careers and MBAs and slightly more students preparing for careers in elementary and secondary school teaching, nursing, and other fields where the monetary rewards are smaller but the contribution to society is arguably no less and very likely greater.

(7) Under an UDIC loan program, students pay for their own education as the benefits from that education become manifest. In most cases, this will reduce the

major financial burden on parents and shift much of it to their children who benefit directly from the educational investment.

(8) By setting repayment rates and the length of the repayment period appropriately, a UDIC program will be self-financing, thus reducing or eliminating any subsidy from the taxpayer.

(9) Finally, if UDIC loans are successful to the point that students favor them over the Stafford and Perkins loan programs, the federal government will save up to $5.1 billion of federal education spending per year. These dollars—or at least a portion of them—could be used to expand the Pell and SEOG grant programs for the most financially disadvantaged students. There are likely to be other benefits as well: simplified and cheaper administration of education loans is surely one of them.

SOME QUESTIONS ABOUT U-D-I-C LOAN PROGRAMS LIKE IDEA

A loan program as ambitious and "newfangled" as that envisioned in the IDEA plan is bound to raise a number of questions about its funding, its impact on public and private institutions of higher education, and its possible adverse effect on tuition levels. A number of these can be answered here.

Question. Won't the implementation of a large scale U-D-I-C program add too much to what we spend on postsecondary education?

Answer. No, for two reasons. First, a successful UDIC program will simply substitute a better financing mechanism for an inferior patchwork quilt of current funding programs. Second, at least a small increase in higher education is warranted by the high rates of return that college and university graduates now obtain. We are no longer, "overeducated" as was the belief during the 1970's when returns to higher education temporarily waned. One quantitative measure of the value of education beyond the high school diploma is the enhanced earnings that educational investments produce for those who pursue college and university training. My colleagues and I have calculated that in 1990 dollars, the present discounted value of completing some college beyond the high school degree over the lifetime of the average worker is approximately $140,000. The present discounted value of four or more years of college is nearly $500,000. These higher earnings reflect higher productivity.

Question. Won't a UDIC loan program jeopardize public higher education by encouraging students to enroll in more expensive private schools?

Answer. Unlikely. While the repayment rates are reasonable, students will still be forced to pay a significant amount of their earnings over a substantial period of time in loan repayments. As a result, students will not automatically abandon public higher education for higher priced private schools. Likewise, the maximum lifetime limit stipulated on awards in such a UDIC program as envisioned in the IDEA plan force students to be price conscious in making their investment decisions. Moreover, it is not unreasonable to expect that the overwhelming majority of individuals who decide to pursue higher education precisely because of UDIC loans will choose lower priced public colleges and universities, boosting the overall numbers going into the public sector.

Question. Won't a UDIC program lead to enormous increases in the level of tuition and fees?

Answer. Not necessarily. Continued competition between schools for a relatively stable number of college and university students will ultimately require high priced private schools to limit increases in their tuition and fee schedules. This is likely to occur with or without UDIC loans. In any case, if tuition does continue to skyrocket at private schools, the correct remedy is one that is now being implemented, at least tentatively: antitrust action.

Public colleges and universities may be another case. They may use the IDEA program to reduce the size of state government subsidies. Given the interstate mobility of students after graduation and the subsidy of middle class students on funds raised by regressive state taxes, increases in in-state tuition may, in fact, be justified. In an era of restrictive state budgets, UDIC loans would relieve states of some of the tuition burden. Yet, in order to maintain a "good business climate", one can expect state legislatures to maintain relatively low college and university tuition and fee rates in order to provide strong incentives for their citizens to pursue what is presumably productivity enhancing higher education.

Question. What keeps unscrupulous operators from setting up "sham" training schools to take advantage of UDIC-funded students?

Answer. The IDEA program requires that institutions eligible for federal loans be fully accredited and licensed by the states within which they operate. Moreover, the IDEA loan authority could be given oversight authority to do spot checks on state accreditation and licensing. To keep tuition and fees in line, the cost of education could be made one criterion for determining inclusion of a particular institution in the IDEA demonstration.

Question. Won't the initiation of the IDEA program force colleges and universities to spend a much greater effort on administering financial aid?

Answer. No, not necessarily. College and university financial officers are understandably skeptical about any new student loan program, especially one that circumvents the private banking system. They worry that any federal government agency entrusted with administering a UDIC program will go about its business in an inefficient bureaucratic manner, forcing the schools to assume greater responsibility. The creation within the federal government of a special agency or "Trust" to administer the IDEA program can take much of this burden off of the individual school. This would be particularly true in financial officers played a constructive role in helping to develop the regulations for the program. If the regulations are satisfactorily drawn, schools should face no greater burden than under current programs. They, of course, will have to continue to supply the federal government with basic information about enrcllment status and provide a campus-based office where students can receive their loan payments.

Question. How will a UDIC program such as IDEA likely affect low-income students?

Answer. The IDEA plan could end up providing additional resources to low-income students. First, the program permits students to borrow more funds with more reasonable repayment schedules Second, Congress can take a portion of the $5.1 billion now spent on the Stafford and Perkins loan programs and transfer it into the Pell and SEOG grants which have been especially helpful to low-income students.

Question. Will implementation of a federal UDIC program such as IDEA make state college prepayment programs like that in Michigan obsolete?

Answer. No, not necessarily. States which wish to set up college prepayment programs can do so regardless of UDIC loans. Parents who wish to make substantial contributions to their children's education can do so using this mechanism.

Question. Won't the IDEA program have a negative effect on philanthropic contributions to institutions of higher education?

Answer. Probably not. Most corporate and individual giving to higher education is for capital expansion, not current expenses. One suspects that corporations and individuals will continue to contribute to college and university endowments for such purposes.

Answering these questions obviously will not mollify all those who would oppose the IDEA demonstration project. Moving toward such a radical restructuring of education finance will certainly have its detractors. Private banks, subsidized by government guaranteed student loans, will certainly balk at losing this lucrative market. Those who are part of the vast bureaucracy involved in servicing the current array of loans may also object on self-interest grounds to a system that makes their efforts largely unnecessary. However, the gains from implementing a UDIC loan plan like IDEA—from the perspective of students, their families, and the corporate sector advocating more resources for education—presumably should carry the day.

Indeed, it is the rare government program that simultaneously satisfies a number of disparate public policy goals and at the same time has the opportunity to garner broad bipartisan support. The IDEA plan has the potential for being one of these. By providing a significant increase in the level of federal funding available for post secondary education, by appealing to the needs of the middle class student as well as the student from the low-income family, and by providing a prudent investment opportunity for the U.S. Treasury, the IDEA higher education loan program meets both the criteria of efficiency and equity for a government program.

The specifics of the program can be debated and revised, but the basic structure provides a sound basis for promoting the national debate on how America can renew its commitment to education and to equal opportunity. Put simply, expanding on the principles set forth in the IDEA amendments to the Higher Education Act of 1965 could be the ideal way to pay for education in the future.

The CHAIRMAN. Thank you very much.

A number of our members are present, so I'll ask that we try and limit our questions. But let me just ask all the panelists about one of the criticisms that we have not really addressed here today which I think has to be in the minds of many: With this loan pro-

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gram effectively assured, won't all colleges and universities effectively just raise their tuitions to soak it up?

Let's start with you, President Silber.

Mr. SILBER. Senator Kennedy, I don't think that's true at all. As I said, this year, Boston University increased its tuition and fees and room and board a total of 2.9 percent. Our restriction was on the ability of students to pay. With a 22-percent increase in the number of students qualifying for financial aid, and with no increase in the availability of financial aid funds from the Federal Government, we had to increase out of our own budget the student financial aid by $15 million, and next year it will be $12 million. If we had a program like this, if it meant any difference to us at all, it would mean that perhaps we could increase our own student financial aid budget by perhaps $4 to $5 million instead of $11 or $12 million. It would be a help to the university; it would, if anything, enable us to hold the price down, not to gouge on it.

I don't think the record will show that the universities have simply been gouging by raising tuition. The problem is we live in the first period in human history in which intellectuals had a market value. If you went back 60 years ago, mathematicians were a dime a dozen; they were about as useful as poets. And the only people in those days who ever were hired at any great salary were people like chemists, who could testify in a casualty suit and get a good fee from a lawyer, or they worked for Dupont or something like that, and figured out how to blow somebody up.

But basically, intellectuals like people in the English department, people in philosophy departments, math departments and physics departments had no market value. Now they have enormous market value. People even in English can be hired off to Madison Avenue as writers and do very, very well.

So we are out there competing with the market. And of course the Congress has done very well in raising the price of lawyers. When I came to Boston University, a full professor of law, a distinguished professor of law, earned less than $30,000 a year. Now, if you want to hire a brand new lawyer right out of law school with 2 or 3 years' experience, you pay $75,000. And for a distinguished professor, you'd pay $125,000.

This is the marketplace that we have had to make. We didn't invent it. Intellectuals have a market value. That's what is driving up the costs.

Mr. BLUESTONE. If I might add a statistic or two to this, the University of California at Los Angeles carries out something called the American Freshman Survey. In 1979 when they carried that out, they found out that 11.3 percent of all freshmen in the United States at 4-year schools were receiving grants or scholarships that were funded by the college or university where they attended; 11.3 percent in 1979. In 1989 when they carried out the same survey, that was up to 20.3 percent. I think this confirms a point that President Silber was making.

The second thing has to do with not private education, where in Dr. Silber's case you are talking about education which costs in excess of $20,000 a year, but the University of Massachusetts at Boston where our tuition and fees have risen, as I said, double, to about $4,500. We are seeing, given our students, who come generally from the working class of the Boston area, that we have reached the elastic part of the demand curve. That is, as we have raised those tuition and fees to try to keep the university afloat, we are seeing the number of students coming and applying to the university declining. We have lost 900 new students this year alone as a result of that rise.

So that I think this question of what keeps tuitions from going up too fast is indeed the market, and that is going to be true throughout the system.

Father BRYON. I don't think it necessarily would happen. If this proposal goes through, it is going to introduce some new competition into the marketplace. We look at cost and price, always making that distinction. In the independent sector we have higher prices than the State-subsidized sector, but not necessarily higher costs. And we are going to be seeing ourselves staying competitive one with the other with some price discipline as well as cost discipline.

Nobody could give you a guarantee that there wouldn't be some price increases. There have been price increases in the past, but those price increases are going to be geared very, very tightly to the costs, over which some of those we have no control.

Ms. HOOYMAN. I would echo that in saying that I believe from my perspective it is a much more positive marketing stance if we are able to say to a family, "We have contained our cost increases to 6 percent this year," rather than saying, "We've increased our costs by 12 percent but, boy, do we have a great loan program for you." That would be my perspective.

The CHAIRMAN. Thank you.

Senator Kassebaum.

Senator KASSEBAUM. Dr. Bluestone, I'd just like to commend on your observation about the health care system because the health care system, as it spun out of control and cost, has only invited the Government in to try to impose controls. We began with hospitals, and now we're trying to assess how far we should go with both the insurance companies and the providers, the physicians. I think you could make some comparisons, as a matter of fact. As costs of higher education seem to go beyond control, with Federal dollars involved, we are going to try and impose more and more controls.

So I think it is an apt comparison, but I'm not sure that the end result is one that, as a matter of fact, we want. That is my concern about this issue in trying to figure out how best to work with the student loan programs.

I agree there is a wide variety of loan programs. Am I hearing you say that you wish we could combine all of these into a single loan program?

Mr. BLUESTONE. I said, Senator, that ultimately, particularly with this demonstration, that students are in some sense going to march with their feet. They are going to try and move toward those loan programs that work effectively.

If this one doesn't work, it is going to disappear. I think what would happen, and what I would ideally like to see—maybe it won't—is that over time we'll see certain of these programs rise to the top as they have with the Stafford loan program, which dominates the others in terms of total size, and it is possible that this program in the future might be one of the largest of all the programs because it is the best one from the point of view of the Government and the best one from the point of view of the students.

Senator KASSEBAUM. Earlier on I asked about expanding the SLS because, essentially, this is what we're talking about. Would that have any merit, or should we do away with SLS if we are going to move in this direction?

Father BRYON. I mentioned the SLS in my testimony, but you weren't here then.

Senator KASSEBAUM. I apologize. Alan Greenspan was just talking about the shape of the economy.

Father BRYON. How are we doing? [Laughter.] But I pointed out that for purposes of this demonstration—your concern was one with an additional entitlement—I suggested that those who are drafting the legislation might consider a trade-off. For an institution that goes into this demonstration set, this group, they might be willing to trade off access to SLS in order to have this, and thus there would be no entitlement problem, or at least no alteration of the entitlement equation, through the life of this program.

On the health care thing, we don't have any system of educational insurance in the United States and the third party payers, all of which are there, and every time mention is made of a Government program, those of us who are running the places always hear that you are going to have the Government all over you, and you're going to have all of that interference.

Well, I have been in higher education administration for 20 years now, through a whole lot of programs, and I can honestly say I am happy to live with that situation, and I have not experienced the oppression of Government regulation or telling us what to do.

I'd sure be willing to run that risk if we could get this program in place because this program is for the benefits of our students, and that is why we are there in the first place.

Ms. HOOYMAN. I would concur in that. I feel that it could very well serve to replace the current SLS program. In fact I would recommend that were an institution to volunteer to participate in this program, that would make them immediately ineligible to participate in the SLS. I feel it would be very effective in serving our students, so I see that as a natural outcome.

Senator KASSEBAUM. One other question regarding Senator Pell's observation that, if we use the Treasury as a means of collecting on the new program, it should be used for all student loan collections. Otherwise, there really is discrimination that enters in; have you made any comments on that observation?

Ms. HOOYMAN. Are you asking for all current GSL programs? Is that what your question is?

Senator KASSEBAUM. I assume that was Senator Pell's observation, was it not?

The CHAIRMAN. I think that is the point he makes on it. I think if we're talking about doing a demonstration or a pilot program, as far as I'm concerned, that we ought to have it be a demonstration or a pilot program, and not tie it back into the other programs. But I think it does have the inherent problem in terms of the enforcement mechanism, which we would have to consider at the time of evaluation.

Senator KASSEBAUM. And some discrimination between students who are borrowing for real need and those whose job possibilities might be a bit different.

I have used up my time. Thank you.

Mr. BLUESTONE. Senator, I don't have a definitive answer for your question, but I think obviously the drafters have to think about this problem.

I think to the extent that students would have an opportunity, almost cafeteria-style, to go with one system rather than another, there are going to be pluses and minuses attached to each one of them. The current programs, for example, do have a very large interest subsidy. This one has none at all. What that would mean is that you are going to have on the one hand students seeing some benefit to going with the current program.

On the other hand, the repayment system if you think about it has kind of a built-in insurance system to allow them to pay it on an income-contingent basis. This will be attractive to a lot of students, and so as a demonstration project what we would be able to do is to see who elects which program and why, and to the extent that we will also be studying this, it will give us an opportunity to craft improvements in that legislation.

Let me just go back to one other point you raised, though, because I think you were raising it with me, and that had to do with the health insurance as an analogy to higher education. I think most people in the health field—and I admit I'm not an expert in that area—would argue that a great deal of our added cost and why we are spending such a higher percentage of our gross national product on health care has to some extent to do with the fact that we're using private insurance to fund a great part of our health insurance, and that means very, very high administrative costs.

That is also the problem we have in higher education today, that by developing the system and using banks and third party payment, we actually add an enormous amount of administrative cost which doesn't benefit the taxpayer or the student, and we have to deal with that.

Senator KASSEBAUM. I know I shouldn't, but let me follow that up for a moment. I understand the fastest-growing part of university budgets, as a matter of fact, is in administrative costs; is that true?

Mr. SILBER. No, it isn't true. It depends upon the university. I think if you take a look at some of the universities, at the University of Pennsylvania, for example, I believe the ratio of faculty to nonfaculty positions is one faculty member to seven others. If you go to Boston University, you'd have one faculty member to about 1.8 nonfaculty members. So it varies enormously between institutions and depends upon the efficiency with which they are driven.

The same thing is true of secondary education. If you go to the Catholic schools, they are very lean in administration and very long in the teaching staff. The bite-to-tail ratio there is very favorable. But if you go to a typical school system, it is loaded with nonproductive administrators and relatively few teachers. So there is no generalization there.

Senator KASSEBAUM. That's just a very objective observation. [Laughter.]

Mr. SILBER. Indeed it is, Madam Senator. It is quite objective, and there is all kinds of data to back it up.

Senator KASSEBAUM. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Simon.

Senator SIMON. Thank you, Mr. Chairman, and I thank all of you.

Let me just add this thing is evolving, and you may on reflection have other ideas. I might just mention, Dr. Silber, that we used a 6-percent Treasury rate, which is slightly higher than the CBO projections, but all of these things can change.

I thought your comments, Mr. Bluestone, were absolutely on target. We are talking about an investment entitlement rather than a consumption entitlement, and I think that is a huge, huge difference, and one that will ultimately pay back for this country.

John Silber, you have been known for being tart-tongued and blunt, and you have not let us down today in that respect. Let me ask you this question. We have opposition to this, obviously, by the banks, for reasons I understand. One of the institutions we created to help students is Sallie Mae, and they have helped students, but they see this as a threat to their institution, and they are spending money lobbying against this legislation.

Do you have any suggestions for us in that area?

Mr. SILBER. Well, I think that crass form of influence-peddling should be looked down upon not only in candidates for public office but particularly in Government agencies. I think it is scandalous that they can spend the taxpayers' money trying to perpetuate their own empire, and I think the idea that banks are not a special interest is ludicrous. The idea that banks want to make enormous profit off a guaranteed loan, where the basis for a profit in banking is based on risk-taking, and they have zero risk on the loan—that should reduce their margin substantially. But they don't want to reduce their margin, and consequently it is a highly profitable venture. Well, I can't think if any reason why a bank wouldn't fight to keep a bird's nest on the ground when they have one, but there is no excuse for allowing them to do it. I think it ought to be exposed for the sheer special interest lobbying that it is.

Father BRYON. About 40 years ago Eric Sevareid wrote a book, and the title of it was *Not So Wild a Dream*, and he took the title from a quotation of Norman Corwin, who was speaking about brotherhood—we could apply it to direct lending here—which was: "Brotherhood is not so wild a dream as those who profit from postponing it pretend."

Senator SIMON. I like that quote, and I can't think of a better way to end my questioning.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Durenberger.

Senator DURENBERGER. I'll pass, Mr. Chairman.

The CHAIRMAN. Senator Bradley.

Senator BRADLEY. Thank you very much, Mr. Chairman.

Let me first of all thank all four of you for your testimony and thank the chairman for allowing me to sit in the hearing today.

I wonder if you could describe why you think it is an advantage to try to develop a program that allows nontraditional students access to a college education—meaning not 18- or 19-year-olds, but those who now under existing programs have difficulty getting access to financing for a college education.

Mr. SILBER. I think for one thing, Senator, there is no way that you can know in advance of the educational opportunity, the full intellectual capacity, spiritual artistic capacity of individuals. We discover the limits of our capacity by testing them, and a good college or university is a place that gives individuals the opportunity of testing the envelope of their own capacity. And you don't know until they've tried. This is an important thing to encourage.

I am influenced by this regard by the fact the my mother, in her thirties, while she was teaching full-time had to go back to school to become a fully-qualified teacher because she was supporting our family, and without her income we simply would have had no way of surviving. Her access to education was based on night school and summer school, and these are the kinds of educational opportunities you are talking about. But it was a grave burden for her and for the family for her to complete that education.

I think today it is even more serious when you have single-parent families who are stuck on welfare, and the mother may not have the skills to get a job. To open the doors of higher education and the doors to greater economic productivity for such individuals is extremely important. This is one way we can reduce the cost of welfare is by truly empowering individuals who are on welfare—and empowerment doesn't mean putting your hand into a fist and raising it menacingly at somebody else; empowerment really has to do with the ability of an individual to do more things than they could do before, and educational institutions provide the greatest opportunity for the enhancement of their capacities.

Father BRYON. We are in the business of the development of human potential, and that potential doesn't dry up at age 22 or 23; it is there through life. We all get plenty of resumes these days by people who are sidelined by the recession, and it would be great if they could go back to school. Some of the more entrepreneurial institutions are giving free tuition for graduate work for those alumni who are temporarily sidelined.

Senator BRADLEY. These are people who are essentially out on their own now, and parental income for them as a concept for eligibility is irrelevant; right?

Mr. BLUESTONE. It's meaningless. I'm not sure I even like the term "nontraditional" anymore because our higher education institutions are changing. At my university, the average age of our students is now 27. I would say it is probably true that 70 percent or more of our students are self-financing their education not based on their parents.

Second, we keep talking about lifelong learning, the need to go back to school sometime later in life to learn a new occupation or learn a new skill. I happen to have grown up in Detroit, and I feel acutely the fact that General Motors yesterday announced the closing of 11 plants, with 16,000 additional layoffs. By 1995 General Motors will have half the employees it had in 1985. What happens to those people? Where do they get the education and training in order to become productive again in the American system?

This program would give them an opportunity that in many cases they do not have today.

Ms. HOOYMAN. I would add from my perspective that I find this particular group of students probably to be the most highly motivated group of students that I know.

Senator BRADLEY. The most self-reliant.

Ms. HOOYMAN. Yes. They have seen enough of life experience that they know what they want. And unfortunately, given the fact that they are older, many of our more traditional institutions are not very well serving that particular population and are in dire need.

I would add that in Michigan, for example, our legislature has found that there is increasing demand on our State aid programs largely due to the growing influx of the nontraditional older student, so they are really being hurt in the process.

Senator BRADLEY. If I could follow up on some of the points that were made by the panel about what should be the design of the 5-year demonstration, the question really is should you make self-reliance loans another way to pay for college education, voluntarily chosen on the part of individuals, or should you require anyone who takes a self-reliance loan to be ineligible for any of the others?

Dr. Silber, you had a clear point of view on that, and I was wondering if other people on the panel have any thoughts about that. Then I would like to come back, Dr. Silber, for your suggestion about something.

Father BRYON. I'd be inclined to say give them the choice, and if they choose the self-reliance, go that route. I think that is the whole point of the demonstration so that we can in fact prove that they are better off having gone that route and that the Nation would be better off if that were the more commonly used means of financing student aid.

Mr. BLUESTONE. I agree.

Ms. HOOYMAN. My ideal would be that we not necessarily add another loan program and use the structure that we currently have. However, if we were to go this route, I would just say that I would prohibit the student from looking at the SLS loan, to still have access to the Stafford loan program, just because of the attractiveness of that particular program, but that they would not borrow under SLS.

Senator BRADLEY. That any student would probably go to the Stafford loan first because of the in-school subsidy.

Ms. HOOYMAN. Yes, much more to their benefit.

Senator BRADLEY. It's a much more attractive route, so probably they would go that route anyway, until they exhausted their eligibility or their funding level, and maybe then they could move to the alternative, self-reliance loans.

Ms. HOOYMAN. Exactly.

Senator BRADLEY. Dr. Silber, you raised a question about if we had self-reliance loans in a model that also allowed Guaranteed Student Loans or Pell Grants. You were concerned that the repayment rate, which in the bill is Treasury bill plus two, would create a very serious burden over the long-term, and you pointed out the Treasury bill plus two rate over the last 20 to 30 years.

What if we didn't use T-bill plus two, but rather we used the long-term borrowing rate—say, the 30-year Treasury bond?

Mr. SILBER. The 30-year Treasury bill right now is almost 8 percent.

Senator BRADLEY. But this is an historical anomaly. We are in a period where the normal, which is the long rate is higher than the short rate, is an extremely unusual thing, so the reverse of your point is probably valid.

Mr. SILBER. Well, if you are going to be guessing, but you are trying to reduce the amount of the interest rate, why don't you just peg it so you really know what it is going to be? If 6 percent makes it work, then peg it at 6 percent. If 7 percent makes it work, peg it at 7 percent, and not bother with it.

But the point I was making is that there is a reason, I believe, why we had a large number of sponsors for the legislation that Senator Kennedy introduced back in the late Seventies and why Senator Kassebaum was willing to support it—it is a different and better proposal than this one. And I think a pilot program based on that proposal could be made into a coherent program, and it would work. I think this one is so deeply flawed in various ways that it is not a genuine pilot program; I think it is a crippled pilot program that will embarrass us by its consequences. I think it has flaws built into it that it will be very difficult to correct; whereas I think you could substitute for it as an amendment to this piece of legislation a pilot program based on that original legislation of 1979, and it would work beautifully at no greater cost.

Senator BRADLEY. Just to follow up on the point that you made, would we really be better off if we did the long-term borrowing rate versus the Treasury bill rate, given the predictability and the difference in—you cited the T-bill plus two rate as 9 percent over 20 years whereas the long-term borrowing rate over 25 years is probably around 7 percent.

Mr. SILBER. Well, I like 7 percent better than 9.6; that's true.

Senator BRADLEY. OK. Thank you.

The CHAIRMAN. If I could, Mr. Bluestone, it used to be at the University of Massachusetts that 85 percent of the kids' parents never went to college and 85 percent of them worked 25 hours a week or more. Is that still pretty close to it?

Mr. BLUESTONE. I don't know the exact number, Senator, but I think it's fairly close to that.

The CHAIRMAN. It's an extraordinary group of young men and women.

I want to thank all of you. Clearly we're going to be back in touch with all of you as we move through this whole policy issue. There is enormous energy and interest, and I think all of us are impressed by the genuine strong desire to give assurances to young people of access to higher education. We're going to try and work through this and respond to a lot of the kinds of questions that were raised today.

We are enormously grateful to all of you who have given a lot of time to this and have been very, very helpful and positive certainly to me, and I think the record will show, to the other members as well.

Thank you very much.

We have one final panel, and we very much appreciate their patience in waiting. If they would all come forward now.

Roxie LaFever is the vice president of financial aid at the University of Phoenix; Jerry Davis, vice president of research and policy analysis, Pennsylvania Higher Education Assistance Agency; and Michael Bigelow, deputy assistant commissioner for returns processing at the IRS.

At the outset, I want to apologize to you for a scheduling conflict that I have. I think most of us felt that our first panel was enormously interesting, and we may have gone on longer than we had earlier anticipated, but Senator Simon has been good enough to indicate that he will chair the remainder of this hearing.

I do personally want to thank all of you very much. Some of you we have had the good opportunity to have worked with in other aspects of education programs, and we are very grateful to all of you for being with us here today.

I'll recognize Senator Simon, who will chair the rest of the hearing.

Senator SIMON [presiding]. Ms. LaFever, please proceed.

STATEMENTS OF ROXIE LAFEVER, VICE PRESIDENT, FINANCIAL AID, UNIVERSITY OF PHOENIX, PHOENIX, AZ; JERRY DAVIS, VICE PRESIDENT, RESEARCH AND POLICY ANALYSIS, PENNSYLVANIA HIGHER EDUCATION ASSISTANCE AGENCY, HARRISBURG, PA; AND MICHAEL S. BIGELOW, DEPUTY ASSISTANT COMMISSIONER FOR RETURNS PROCESSING, INTERNAL REVENUE SERVICE, WASHINGTON, DC, ACCOMPANIED BY JIM HELM, DEPUTY ASSISTANT COMMISSIONER FOR COLLECTION

Ms. LAFEVER. My name is Roxie LaFever, and I am the vice president of financial aid at the University of Phoenix.

Senators, as a financial aid administrator, I have been very actively involved with the State, regional and national associations. Today I am here to discuss the many concerns and unanswered questions regarding income-dependent education assistance, also known as self-reliance loans.

Although I am speaking on behalf of the University of Phoenix, these concerns are shared by many of my colleagues from all institutional sectors. These concerns and questions are outlined in detail in the analysis submitted, which I would like to have made part of the record.

Senator SIMON. It will be made part of the record.

[The document follows:]

CONCERNS AND UNANSWERED QUESTIONS REGARDING INCOME DEPENDENT EDUCATION ASSISTANCE (IDEA) aka SELF RELIANCE LOANS (Version 4)

Prepared By:
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REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
General Concern	Access to Aid and Education	Depending upon the institutions selected to participate in the Self Reliance Program and the level of participation at the institution, the portfolio mix required (4-year, 2-year, proprietary) for additional secondary market funding (bonds) for the GSL Program may be jeopardized. A decrease in 4-year Public GSLP volume would restrict aid availability for all institutions within given states.
General Concern	Institutional Competition	By establishing a new loan program available to only 300 institutions (selected by the Secretary) until 1997, equity in financial aid packaging is jeopardized creating a situation of unfair competition.
General Concern	Institution Sample Size	Although the Secretary can select up to 300 institutions, the funding level established for each fiscal year (FY94 = $450 Million) may not support a sufficient sample size, i.e. one institution with a large loan volume ($40 Million) could absorb up to 10% of the appropriation. Is the Secretary going to specify a method of projecting institutional funding levels to ensure consistency of information being reported by institutions?

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
General Concern	Lack of Administrative Expense Allowance	Institutions are being asked to assume major administrative burdens without financial support from the federal government to offset the costs of the program. During times of nationwide institutional budget cuts, institutions cannot afford to assume these costs. On the other hand, institutions cannot afford to turn away from a major new source of federal funds for students. (Catch 22)
General Concern	Funding Sources	By establishing an additional loan program, will funds be drawn away from other financial aid programs in future appropriations? Furthermore, the bill defines this loan as a contractual right (entitlement) to the student against the United States in section 453 but also sets funding limits by fiscal year. How is the cost of this program being offset in the budget? A separate amendment attached to Version #4 indicates that: 1) funds must be "raised or earmarked for deposit into a new or existing trust fund to be used for this purpose," or 2) reduce direct spending authority elsewhere. When passing the Act to provide funding for this program, Congress needs to provide sufficient lead time so that the Secretary and selected institutions are able to properly plan and implement the program
General Concern	Responsibility for Borrower Notification	At what point does the Secretary assume responsibility for notification to the borrower of critical changes in information concerning the student loan, i.e. changes in repayment schedule, updates of interest rates, etc.

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
General Concern	Unjustified Tuition Inflation	If the borrower's outstanding balance is written off after 25 years of repayment (maximum 7% of income), abusive institutions may inflate tuition costs unjustifiably since default rates and negative credit impacts will no longer be an issue. The latest version has added a requirement for DOE to evaluate the impact of SRL on tuition costs. Since institutions do not currently report a cost of attendance for loan eligibility (only Pell which would be misleading), how will the Secretary be able to analyze tuition costs without requesting further documentation for schools - again administrative burden.
General Concern	Spouse Assumption of Debt	The language is unclear whether a spouse assumes responsibility for the borrower's debt. If yes, does this assumption conflict with community property laws established by states in the event of a divorce?
General Concern	Development of Regulations	Negotiated Rule-making and Proposed Regulations should be required as part of the Secretary's regulation development for implementing the Self Reliance Loan Program.
General Concern	Fiscal Year vs. Academic Year	Under this amendment, all reporting and cost of attendance calculations are requested on a fiscal year basis instead of academic year. This change requires an institution to analyze a stud[illegible] [illegible]bility with two separate calculations and report to the governm[illegible] [illegible]ing two different reporting periods.
General Concern	No Consolidation	By removing the consolidation language in previous versions, the authors undermine the benefits established under consolidation in the GSLP. No option of consolidation requires students to make multiple payments to multiple agencies thereby compounding the confusion and adding to the default problem. Without consolidation, repayment is extremely [illegible]cult for students in academic endeavors that lead to a high debt [illegible]en.

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
Initial Payment Page 3 - (2)	Availability of Funds	The bill stipulates an initial payment time frame of 10 days after the start of the academic year but does not establish a time frame for additional payments assuring access to funds for both the student and the institution in a timely manner. Delays in receiving funds will create cash flow issues since most institutional costs occur prior to the start of an academic year.
Needs Test for Students Page 3 - (b)	Student Eligibility	An eligible student shall not receive a Self Reliance Loan in any fiscal year unless such student's eligibility for a loan under GSLP and Pell has been determined. The language is unclear as to whether this requires a calculation based on a need analysis application. Again, this is based on fiscal year not award year or academic year. However, Title IV aid from all programs cannot exceed the student's cost of attendance.
Expansion of Program Page 5 - (4)	Definition of Administrative and Fiscal Capacity	The manner in which the Secretary defines administrative and fiscal capacity could provide a mechanism to eliminate specific sectors of the higher education community and/or small sized institutions.
Agreement Required Page 6 - (1)	Institutional Liability	The institution is required to sign an agreement assuming full liability for administration of the program. In the GSL Program, the institution shares liability with various parties.
Agreement Required Page 6 - (2)	Monthly Reporting of Loan Recipients	Additional administrative burden will be felt by institutions due to the requirement to report loan recipients and changes in enrollment status monthly. This burden could be minimized by development of a computer system for uploading this information.

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
Agreement Required Page 6 - (3)	Institutional Assumption of Loan Origination, Disclosure, and other Requirements	Many functions of the current GSLP system are invisible to institutions as they are managed by lenders and guarantee agencies. Administrative burdens under SRL at the institutional level will be increased greatly by this requirement. Institutions are currently not familiar with these processes but will be held liable if mismanaged.
Agreement Required Page 6 - (4)	Timing of the Transfer of the Promissory Note	The requirement to transfer the promissory note within 30 days after the origination of the loan could create the following concerns: • Changes required in the promissory note after initial certification • Reporting of subsequent advancement of funds requires amendment of original promissory note • Requirements to cancel and reissue promissory notes due to enrollment status changes • Exceeding fiscal year maximums if student transfers to another institution and the original note is not cancelled in a timely manner by the Department of Education
Agreement Required Page 6 - (5)	Reporting Requirements Established by the Secretary	The additional administrative burden for reporting requirements, as defined by the Secretary, could be prohibitive in light of the amount of other additional administrative responsibilities being assumed by the institution to manage the new program.
Agreement Required Page 6 - (6)	Institution Acting as Agent of the Secretary	Will an institution required to act as an Agent of the Secretary be held responsible for actions of the Secretary or events out of an institution's control, i.e. promissory notes lost in the mail, problems with the repayment process, loss of payments, etc.

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
Agreement Required Page 7 - (7)	Borrower Counseling	Borrower counseling with regard to repayment options for SRL loans is required at such time that the borrower leaves the institution. For GSLP and Perkins students, counseling is required when a student drops below half-time but SRL does not. Can this counseling be performed at the same time as the GSLP and Perkins counseling or must it be handled separately creating an administrative burden?
Annual Limit Page 7 - (1)	Loan Eligibility Based on Fiscal Year	Loan eligibility based on fiscal year versus academic year could reduce eligibility for students who have nontraditional programs outside of the traditional fiscal year cycle (non standard academic terms).
Annual Limit Page 7 - (1)	Annual Loan Limits	When comparing the annual loan limits for SRL and the current GSLP, it is interesting to note that students attending academic years 1-2 and less than full time students (GSLP sets loan limits based on level of enrollment status) have a higher eligibility amount under the Self Reliance Loan. Past history indicates that students in these categories have a higher default level.
Maximum Borrowing Limit Page 8 - (C)	Increased Debt Burden to Independent Borrowers	The language allows students who are independent under SLS eligibility, GSL or SLS borrowers, using SRL funds to have an aggregate debt level $10,000 higher than non-SRL borrowers. For example, undergraduate aggregate of $62,000 instead of $52,000 and graduate aggregate of $125,000 instead of $115,000. Dependent students and parent borrowers are not allowed this opportunity. Maximum SRL amount is $30,000 for dependent students and parent borrowers and $40,000 for independent students (amount included in Part B and Part E loans above). What is the rationale to allow independent students an additional $10,000 debt? If a student borrowed $40,000 and then repays a portion of his Self Reliance Loan, is the student eligible for additional loans?

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
Interest Rate Page 8 - (b)	Variable or Fixed Interest Rate	The language in the amendment is unclear as to whether the interest rate on these loans is a fixed or variable rate. We have heard that its to be a variable rate adjusted on a yearly basis the same as SLS. That being the case, the rate on SRL (52-week T-bill plus 2%) will always be lower than the SLS loan (52-week T-bill plus 3.25%) and during times of low T-bill rates, the rate strongly competes with the current 8% Stafford rate (current estimated SRL rate is 8.16%). Because of these interest rates, the SRL Program competes directly with the current GSL Program and potentially undermines its very existence.
Interest Rate Page 8 - (b)	Interest Rate Cap	There is no mention of an interest rate cap for the program

REFERENCE	TOPIC	CONCERNS AND UNANSWERED QUESTIONS
Repayment Provisions Page 9 - (a)	Repayment on Tax Return or Payroll Deduction	The language is unclear whether repayment will take place annually through tax filing or through payroll deduction The language indicates that a non-tax filer (normally dependent or low income student) does not have to make payments for that year However, working students (nontraditional, adult, etc) whose gross income exceeds IRS guidelines (single-$5,550, married $10,000) would be required to make payments. Re-entry students attending non standard term institutions would be required to continue repayment under Section 456(b)(3) This section would also require students attending short term programs to continue repayment. Both these types of students become more prevalent during times of economic recession and industry lay offs How will the 7 month or 3 month deferment option be documented? Will this also place additional administrative burden on institutions in order to verify the student's attendance status?
Repayment Terms Page 9 (b)(1)	Affect on Take Home Pay	Regardless of whether a student is repaying 3%, 5%, or 7% of adjusted gross income towards their SRL, the impact on take home pay will be approximately double, i.e. 7% adjusted gross income ends up being 15% of take home pay.

REFERENCE	TOPIC	CONCERNS/UNANSWERED QUESTIONS
Repayment Terms Page 9	Student Loses Option to Select Repayment Terms	Under previous drafts, the student was allowed to select a repayment option based on their debt level. These options varied by percentage of adjusted gross income and number of years of repayment. The current draft indicates the Secretary now has the right to establish the length of repayment and percent of AGI. Potentially, this allows the Department of Education to collect additional funds (interest) due to lengthening the repayment period.
Repayment Terms Page 9 - (b)	Potential for Student Negotiation of Repayment Terms	The language in the amendment is unclear as to the availability of a negotiation option to make the program flexible enough to meet the needs of borrowers with extenuating circumstances such as major shifts in income or family hardships.
Repayment Terms	Readjustment of Payment Amount	Prior versions included the ability for the Secretary to adjust repayment amounts if the student deferred and thereby accrued interest for six years while attending school. We question why this was removed. The removal lessens the ability for the loan to be paid off within 25 years.
Length of Repayment Page 10 - (4)	Program Costs Due to Potential Write-offs	The cost of the program could exceed current expenditures for defaults if the intent is to write-off outstanding balances following the 25 year repayment term.
Deferral of Interest Page 11 - (c)	In School Payments	The language is unclear as to whether a student must make principal payments while in school.

REFERENCE	TOPIC	CONCERNS/UNANSWERED QUESTIONS
Joint Return Page 11 - (e)	Change in Marital Status	The language is unclear as to the impact on payment amount based on joint tax returns if the borrower separates or divorces.
	Avoidance of Repayment	If repayment amount is based on the greater of 1/2 of the joint income on the tax return or individual's AGI, a married student who is not working could get around repayment by filing separately.
Bankruptcy Page 12 - (1)	Bankruptcy Discharge	Why has the prohibition from bankruptcy discharge not been extended to all Chapters of the Bankruptcy Law? The language only prohibits discharge under Chapter 11.
Bankruptcy Page 12 - (2)	Postponement Due to Chapter 11	The language allows the Secretary to postpone (in essence forbearance) amounts required to be repaid for periods preceding the date of discharge. No explanation has been given to the time frame of postponement or to the affect of the 25 year repayment deadline and the potential amount that would have to be written off during the 26th year. Does interest keep accruing during this postponement period?
Central Data System Page 13 - (e)	Timeline for Central Data System Implementation	The timeliness of Central Data System implementation is a concern given the fact that institutional selection must be made by 5/1/93 with the assumption that the program will be fully operational for the 93/94 award year.
Standard Forms and Data Format Page 14 - (f)	Timeliness of Development of Forms and Data Format	The development of standard forms and data formats must be accomplished within a time frame which provides the institution the opportunity to revise procedures and reprogram computer systems before the start of the award year and/or implementation of the Program.

Ms. LAFEVER. Thank you.

In the area of administrative burden, the level of institutional administrative burden associated with this program is excessive. Under this program, all reporting and cost of attendance calculations are requested on a fiscal year basis instead of academic year. This change requires an institution to analyze a student's loan eligibility with two separate calculations and report to the Government using two different reporting periods. Institutions must submit monthly reports on the number of recipients in this program and also any status changes. Institutions must review the promissory note, cut the checks, disclose the terms of the loan, etc. All of these functions are currently being performed by lenders or guarantors underneath the current GSL program.

Institutions must transfer the promissory note within 30 days of origination of the note, which creates numerous problems which are also outlined in my analysis.

Institutions must provide any other reports to be established by the Secretary in the future. These as yet are unknown

Although some schools have Perkins loan moneys already and are used to administering smaller loan programs, most schools have not administered a loan program and definitely not one of this magnitude. However, in order to participate in this program, the institution must indicate that they accept any liability stemming from mismanagement of this program—a task that is new to their experience.

Institutions are being asked to assume major administrative burdens without any financial support from the Federal Government to offset these additional costs. During times of nationwide institutional budget cuts, institutions cannot afford to assume these additional cost.

Funding source. I have several unanswered questions regarding funding; many of them have already been discussed today.

How will this program be funded? Will funds be drawn away from other financial programs that are currently in existence? Will funding become available with sufficient lead time so that the Secretary and selected institutions can properly implement this program? Is this a true entitlement program, and if so why have maximum fiscal year funding levels been set?

Administrative costs to the department will need to be funded through the appropriations process, competing directly with funding for the current title IV programs.

Until these questions are answered and our students are assured that adequate funding will be available without endangering the existence of current grant programs and jeopardizing the current structure of the current Part B loan programs, I believe the Senate should not proceed further.

Availability of funds. The amendment indicates that the Secretary shall make initial payments under this program not later than 10 days after the start of an institution's academic year. If an institution has multiple academic years due to nonstandard terms, are there any assurances that initial payments will b available 10 days after the start of each of those academic years throughout the award period?

Also, what about assurances of subsequent payments for second disbursements to loans? If funds are not available at the beginning of each payment period, institutional cash flow will be negatively impacted.

Due to the size of this loan program, if funds are delayed for several weeks, which often happens in the current Pell Grant program, an institution's financial stability could be jeopardized. Most institutional costs take place prior to the start of an academic year.

The potential cost of the program. Although some people believe that a direct lending program will save the Government money, I am concerned with the costs which will hit in 25 years. This amendment contains several issues which may encourage a borrower not to repay or delay payment, creating a write-off after 25 years. Since the repayment amount is based on the greater of one-half of the joint income on the tax return, or an individual's suggested gross income, a married student who is not working can get around repayment by simply filing separately.

The Secretary can postpone repayment amounts due to the filing of Chapter 11 bankruptcy. However, there is no explanation that has been given to the time frame of postponement or the effect on a 25-year deadline.

By removing the consolidation language that was in previous versions, a student is forced to make multiple payments to multiple agencies if they operate under both loan programs. If a student cannot afford these multiple payments, he will probably default on the Guaranteed Student Loan since the IRS collects on the SRL.

Non-tax filers do not have to make payments if their income is not at the level that they need to file. Since balances are written off, an unscrupulous institution could raise tuition costs and increase student debt without worrying about default rate. That question previously came up. Again, I believe unscrupulous institutions would do this, but of course, not all institutions.

Please take the time to read all of the concerns and the unanswered questions that are in the ten-page analysis that I have given you. I can't take the time here to present all of the concerns, but because of these issues I must strongly request that Senators vote against this amendment.

Thank you.

Senator SIMON. Mr. Davis, we're pleased to have you here with us.

Mr. DAVIS. Thank you.

I am Jerry Davis, vice president for research and policy analysis for the Pennsylvania Higher Education Assistance Agency. We are the agency that administers State financial aid programs and guarantees Federal student loans in the Commonwealth. I am pleased to offer testimony on the income-dependent education assistance proposal.

I have submitted written testimony and would like it included in the record.

Senator SIMON. It will be entered in the record.

Mr. DAVIS. I will just summarize what I have said in that written testimony.

I have several thoughts about the proposal, but I want to focus my remarks on how it would affect student borrowers. I am generally opposed to income-contingent or income-dependent loan programs. The first problem with them is that the borrowers do not and cannot know how much it will cost them to repay their loans at the time they accept them. If they cannot know this, then they cannot know how much their education will cost. If they cannot know what their education will actually cost, then they cannot make intelligent and informed cost-benefit analyses; they cannot assess the relative value of attending institutions of widely different costs because they cannot compare the net costs, that is, the costs after financial aid, of alternative choices.

For over 30 years, those of us in the financial aid community have tried to provide students and parents with better information on college costs and financial aid so that they will consider college affordable and make wise decisions about attendance options.

Income-contingent loan programs are not easily described or understood, especially when a key factor is unknowable—future income. Virtually all income-contingent loan programs encourage borrowers to encourage larger debts than fixed payment programs. IDEA is no exception. Larger debts are encouraged because payments frequently are believed to represent smaller proportions of the borrower's income upon graduation when earnings are lower. But smaller loan payments made over many more years ultimately means that the total payments for a given amount borrowed will be greater than the payments made for a fixed payment loan such as the Stafford loan.

It is impossible to escape the mathematics of the PRT equation—principal times rate times time—unless at some point interest is foregone, a portion of the principal is forgiven or time collapsed. When student loans cost more, then so does the education purchased with them, regardless of the fact that paying for the education is spread over many more years.

Increasing the cost of education does not help us achieve the three basic goals of financial aid—enhancing access, choice and retention. Income-contingent loans are offered as a way to handle borrower debt burdens, to make it easier to afford the monthly or annual loan payments. But the evidence in my written testimony indicates that only about one-fourth of today's baccalaureate graduates would have debt burdens even if all had borrowed the typical amounts of Stafford loans, around $10,000, for their undergraduate years. Many more borrow less than $10,000 than borrow more than that amount.

Debt burdens are not skyrocketing. Pennsylvania's Stafford loan recipients—and I emphasize this—whose access to loans is not restricted by financial need as it is in other States—we have a non-subsidized Stafford loan program—our Pennsylvania student borrowed about the same proportion of their total costs in Federal fiscal year 1991 as they did in 1987.

I might mention here that I am not as sure as many of our speakers are today that college costs are soaring beyond reason. We looked at our Pennsylvania data over the decade of the Eighties, and in Pennsylvania, where I think our costs run any year—we are either second or third highest in the Nation, depending on what some of the New England States do—but our costs increased at about the same rate as our family incomes increased in Pennsylvania during the 1980's, and the costs were absorbing about the same proportion of the family incomes in 1989 as they were in 1980.

Another problem when we talk about the middle income student is that I think their plight, while it is of great concern to my agency as it is to you, may be overexaggerated. I think it may be overexaggerated because we have seen that postsecondary education participation rates in our State, in other words, the number of high school seniors who are graduating and going on to school in our State and in almost every other State in the Union during the Eighties, have gone up.

If college costs were unaffordable to the majority of the people, and it was becoming increasingly difficult to pay for college costs, you would think the participation rates would have fallen. But I digress.

Some believe that income-contingent loans will solve the default problem. I think this is wishful thinking. Borrowers default on their loans primarily because they don't have enough money to make their loan payments. The education and training defaulters paid for with loans did not sufficiently enhance their ability to earn enough additional money to repay their loans. And this generalization applies at all levels of postsecondary education.

Income-contingent loan programs assume that all borrowers will have incomes, but in 1989 7 percent of the 4-year college graduates—this is not community college or vocational trade schools; these are 4-year college graduates—7 percent of them between the ages of 25 and 34 had no earnings, and another 16 percent earned under $12,000.

Giving students income-contingent loans will not ensure that they have incomes. Borrowers might not be able to default on an income-contingent loan, but they certainly cannot repay them, and either way it costs the Government money.

I want to turn now to some specific considerations on the IDEA proposal. Self-reliance loans are promoted as supporting middle-income students. Now, just because middle-income students may have access to these loans does not mean that they are truly supported—first of all, because there is no in-school interest subsidy, the cost of borrowing will be greater than the cost for a Stafford loan. IDEA borrowers will leave school after 4 years, owing about 16 percent more for self-reliance loans than for similar amounts of Stafford loan.

Second, because the IDEA repayment schedules are based on proportions of borrowers' income and may be extended to 25 years, their repayment costs will nearly always be greater than for Stafford loans in total dollars, and in many cases, proportions of their incomes.

A third reason that the IDEA proposal does not support middle-income students is that their parents can and likely will force the students to borrow against their future incomes rather than support them through their own current expected family contributions. This will have the effect of transferring the costs of education to the generation receiving them, rather than having parents continue to support their children when they are able to do so. The IDEA proposal may support middle income parents but it certainly doesn't support middle income families if you include the student as a member of the family.

Moreover, because we have seen that many college graduates will not earn much money, many will still be paying for their education when they are ready to send their own children to college. If Congress intends to transfer more of the burden of paying for education to the student rather than have parents and the other members of society, through tax-supported financial aid programs, help meet those costs, the IDEA proposal will do that. I don't think Congress should have this goal.

I might mention that one of the witnesses this morning mentioned that parents do not provide money for students. According to the national postsecondary student aid study, they do. This is a study that is conducted by the Department of Education every 3 years.

When I examined the proposal's repayment terms, which require the Secretary of Education to set borrowers' repayment schedules at 3 percent, 5 percent or 7 percent of earnings, I discovered several important weaknesses.

I think if you want to help middle income students, you have the ability to do it without creating a new program by just giving them access to nonsubsidized Stafford loans as we have in Pennsylvania and as is proposed in the House bill.

Thank you.

[The prepared statement of Mr. Davis follows:]

PREPARED STATEMENT OF MR. DAVIS

Good morning. I am Jerry Davis, vice president for research and policy analysis for the Pennsylvania Higher Education Assistance Agency, the agency that administers state financial aid programs and guarantees federal student loans in the Commonwealth. I am pleased to be here to offer testimony on the Income Dependent Education Assistance Program.

I very much appreciate what I assume are primary motivations behind the IDEA proposal: (1) to help middle-income students gain access to loans, (2) to reduce borrower repayment burdens, and (3) by reducing repayment burdens, help reduce loan defaults. I want to address the last two concerns before coming back to increasing access to loans for middle-income students.

Income-contingent loans are advocated on the assumption that loan debt burdens are soaring. Some Pennsylvania data are helpful here. Table 1 shows the changes in average Stafford Loan indebtedness for baccalaureate graduates from our public and private colleges during the past five federal fiscal years. The average debt increased by about 26 percent. Costs increased by over 33 percent in those years. But borrowers who left school in each of the five years had paid for similar proportions of their cumulative costs of education with Stafford Loans, about 27 percent at public colleges and 17 percent at private colleges.

Pennsylvania's college costs are among the highest in the nation, so more Pennsylvanians than students in other states need to borrow to finance their education. While students in other states have their access to Stafford Loans restricted by need analysis, we offer students non-need-based Stafford Loans through our state-funded nonsubsidised loan program. So borrowing is not restricted only to students who can demonstrate financial need for the funds. Therefore, because our costs are higher and access to loans is not restricted, our students' loan indebtedness is higher and must have risen at a much higher rate than did loan indebtedness for students elsewhere. If the average debt grew at a slower pace than average costs in Pennsylvania, then the situation a in other states must be much better. Thus I think it is safe to say that loan debt among the Nation's undergraduates is not skyrocketing, and is likely growing more slowly than educational costs.

We can assume with some confidence that the "typical" 4-year college graduate leaves school today owing around $10,000 in Stafford Loans. Experience and research have shown that when loan payments reach 10 percent of a borrower's gross income, they become burdensome, often leading to default. For how many and what kinds of borrowers might loan payments on $10,000 in debt be burdensome?

Table 2 shows the 1989 total annual money earnings of persons with four years of college who were between ages 25 and 34. Earnings for this age group are particularly relevant, because these are the years most borrowers will be repaying their loans. Note that the average earning was $27,216, but 6.8 percent of graduates had no earnings and another 16.2 percent earned under $12,500. (If you ever wondered why borrowers default on their loans, here is one answer: many of them have no money to make payments.) Average earnings of females were much lower than those of males, $22,247 versus $32,465. And 10.9 percent of females had no earnings, while another 20.8 percent earned under $12,500. So it is reasonable to expect females to have greater debt burdens than males. (There is no evidence to suggest that borrowing patterns of males and females are different when years in school and types of institutions attended are held constant.)

Table 3 displays the estimated proportions of these graduates who would have experienced debt burdens at $10,000 and other levels of borrowing in 1989. If the graduates had borrowed the "typical" $10,000, then 23 percent would have incurred debt burdens; that is, their annual payments would have represented at least 10 percent of their annual earnings. Over seven out of ten graduates with debt burdens would have been females, because females earn so much less than males. They also were five times as likely as males to have had no earnings. About 29 percent of Black graduates would have experienced debt burdens had they been trying to repay $10,000 in Stafford Loans, as their average earnings were less than those of White graduates, $22,420 versus $27,630.

The estimates in Table 3 indicate that debt burdens are more a function of graduates' earnings than amounts borrowed. For example, when loan indebtedness doubles, from $5,000 to $10,000, only 9.6 percent more of the graduates are added to the proportion with debt burdens, 23.0 percent versus 13.4 percent. When loan indebtedness triples, from $5,000 to $15,000, an additional 21.2 percent of the graduates would face debt burdens. In raw numbers of graduates, when loan indebtedness rises by 100 percent, from $5,000 to $10,000, the number of graduates with debt burdens grows by 72 percent. When loan indebtedness rises by 200 percent, from $5,000 to $15,000, the number of graduates with debt burdens grows by 158 percent.

These data have important implications for consideration of income-contingent loan proposals. First, loan indebtedness is not rising as fast as college costs, or as much as many believe. Second, the vast majority of undergraduates are unlikely to experience debt burdens under typical borrowing circumstances now, and within the next five years if loan debts grow as they have in Pennsylvania for the past five years. If the typical loan in five years is $12,500, matching the 25 percent growth of the past five years, then 27.8 percent of the graduates would experience debt burdens—if their incomes remained as they were in 1989. Even if all the graduates borrowed the maximum allowable for undergraduate study, $17,250, only 44 percent would have debt burdens, again if their incomes stayed at their 1989 levels. Over half the graduates, in 1989, could have afforded payments on at least $15,500 in Stafford Loans without incurring debt burdens.

Third, debt burdens are not evenly distributed among all graduates. Females, especially White females, are much more likely than others to have debt burdens, because many have no or relatively little earnings. Black graduates are more likely than White graduates to have debt burdens, because they earn less. There is no reason to expect these situations to change in the foreseeable future, as the gender-related and race-related differences in incomes have been with us for many years.

Because loan debts are not rising to levels that are burdensome for the majority of graduates, and because existing repayment burdens are not distributed evenly among all student groups, offering income-contingent loan repayment programs to all borrowers may be unnecessary and unwise. Offering those students with debt burdens forbearance, deferments, graduated repayment schedules, and, in some cases, loan forgiveness, is a better alternative than requiring all borrowers to participate in an income-contingent loan program.

I am generally opposed to income-contingent loans. The first problem with them is that borrowers do not and cannot know how much it will cost to repay their loans when they accept them. If they cannot know this, then they cannot know how much their education will eventually cost them. If they cannot know what their education will actually cost, then they cannot make intelligent and informed "cost-benefit" analyses. They cannot assess the relative value of attending institutions of widely different costs, because they cannot compare the "net costs," that is, the costs after financial aid, of alternative choices.

Virtually all income-contingent loan programs allow, if not encourage, borrowers to incur larger debts than fixed-payment programs. Larger debts are made possible because payments frequently represent smaller proportions of borrowers' incomes upon graduation, when earnings are lower. But smaller loan payments made over many more years ultimately mean that the total payments for a given amount borrowed will be greater than the payments made for a fixed-payment loan at the same interest rates. It is impossible to escape the mathematics of the "PRT Equation" (Principal times Rate times Time) unless at some point Interest is foregone, a portion of the Principal is forgiven, or Time collapsed. When student loans cost more, then so does the education purchased with them, regardless of the fact that paying for the education is spread over many more years.

If larger loan amounts are available through an income-contingent loan program than a fixed-payment one, colleges may feel freer to raise their costs at higher rates than they have in recent years. After all, if most students are paying most of their costs through an income-contingent loan program and cannot calculate their true "net costs" of education, it is easier to raise the so-called "sticker price" for them.

Some believe that income-contingent loans will solve the default problem. This is wishful thinking. Borrowers default on their loans primarily because they do not have enough money to make the loan payments. The education and training defaulters paid for with loans did not sufficiently enhance their ability to earn enough additional money to repay their loans. And this generalization applies at all levels of postsecondary education. When students borrow small amounts to pay for vocational training and no jobs are available or the available jobs have low salaries, they are very likely to default. When students borrow thousands of dollars to attend graduate school and their consequent earnings do not increase enough to cover the debt, they are likely to default.

Lending students money through income-contingent loan programs assumes that all borrowers will have incomes. As we saw in Table 2, 6.8 percent of 4-year college graduates between ages 25 and 34 had no earnings in 1989 and another 16.2 percent earned under $12,500. Giving students income-contingent loans will not ensure that they have incomes, or incomes substantial enough to amortize their loans.

Income-contingent loan programs can help reduce borrowers' debt burdens when they experience lower earnings. But so can forbearances, deferments, and graduated repayment schedules offered through the current Guaranteed Student Loan Programs.

Defaults can be reduced another way in a fixed-repayment loan program, by simply extending the time borrowers can be delinquent before declaring the loan in default. When the period in which delinquent Stafford Loans had to be declared in default was extended from 120 days to 180 days a few years ago, the numbers of defaulters on loans guaranteed by PHEAA fell by one-third. This is because we had an additional two months to work with delinquent borrowers to bring their loans into good standing—and the borrowers had another two months to solve their financial difficulties.

The best way to reduce defaults is not through income-contingent loans, forbearance, deferments or extensions of delinquency periods, but is by assuring that the education and training paid for with loans is of the highest quality and enhances the student borrowers' ability to secure a good job with an adequate salary. A second better way to reduce defaults is to provide grants rather than loans to students who enter quality programs but have academic, socioeconomic or other disabilities likely to inhibit their success.

When students are "at-risk" there is no social justice in making them bear the majority of the risks of trying to improve their conditions through education paid for with loans when failure and consequent default on those loans leaves them worse off than had they not made the attempt in the first place. Persons who are responsible for providing education and financial aid to the Nation's students should take to heart a primary tenet in the physician's code of ethics: "First do no harm."

Self-Reliance Loans are promoted as supporting the middle-income students and families. Just because middle-income students will have access to these loans does not mean that they are truly supported. First of all, because there is no in-school interest subsidy, the students' costs of borrowing will be greater than if they borrowed a similar amount from the Stafford Loan program. If the students borrow $10,000 in Self-Reliance Loans at $2,500 per year for four years and let the interest accumulate a 6 percent per year, they will owe $11,593 upon graduation. (I chose 6 percent because the current 52 week Treasury Bill rate is 4.01 percent and the proposed Self-reliance Loan interest rate is T-Bill plus 2 percent.) Thus they will leave school owing nearly 16 percent more than they would have owed had they had access to Stafford Loans.

Second, because the repayment schedules are based on proportions of the borrowers' income and may be extended beyond the usual ten years of repayment for Stafford Loans, the borrowers repayment costs will frequently be greater.

When Senators Simon and Durenburger released materials supporting the IDEA Program, they identified four initial-year income levels to cover the majority of students: $9,750; $13,000, $26,000; and $36,000. I think these income levels are reasonably representative of the kinds of earnings undergraduates can expect when they leave school.

I assumed that all students would borrow $10,000 in Self-Reliance Loans as that is about what they borrow in PHEAA's nonsubsidized Stafford Loan Program. Using the three rates of repayment, 3, 5, and 7 percent of annual earnings, I calculated how much it would cost borrowers to repay their loans at different initial earnings levels. (I assumed that all incomes would increase by 5 percent per year.) Table 4 shows the total repayment costs under the different interest and earnings scenarios.

To repay a $10,000 Stafford Loan in ten years requires $15,052 in interest and principal. In eight out of twelve cases the total costs of repaying Self-Reliance Loans will be greater, from 7 percent to 55 percent greater. In the four cases where the costs are lower, they are from 2 to 7 percent lower.

Note that, with one exception, 3 percent of annual earnings, the borrowers with lower initial earnings, $9,750 and $13,000 per year, will pay from 11 percent ($15,052 versus $16,764) to 55 percent ($15,052 versus $23,262) more for Self-Reliance Loans than they would pay for Stafford Loans. The borrowers who only earn $9,750 in their initial years and are started on a 3 percent of annual earnings repayment schedule are the only lower income borrowers who would pay less, because they don't make large enough annual payments to cover their loans' 6-percent interest. Note that when these lowest income borrowers are started on 3 percent or 5 percent of annual earnings repayment schedules they do not repay their loans in full in 25 years. Thus the government has to forgive between $5,622 and $23,281 in loan debt at the end of 25 years. I will remind you here that these lower income borrowers will include the women, minority students, and others I mentioned earlier.

I might note here that, although their total loan costs are lower for Self-Reliance Loans than they would be for Stafford Loans, when the higher income borrowers are repaying on 5 percent and 7 percent of earnings schedules, their debt burdens are greater than they would be for Stafford Loans because the proportion of income devoted to loan payments is larger. Thus for these borrowers the income contingency feature of the IDEA program works to their disadvantage.

A third reason that the IDEA proposal does not favor middle-income students is that their parents can, and likely will, force students to borrow against their future incomes rather than support them through their own current "expected family contributions." This will have the effect of transferring the costs of education to the generation receiving them, rather than having parents continue to support their children when they are able to do so. The IDEA proposal may support middle-income parents, but it certainly doesn't support middle-income families. Moreover, because we have seen that many college graduates will not earn much money, many will still be paying for their education when they are ready to send their children to college. If the Congress intends to transfer more of the burden of paying for education to the students, rather than have parents (and the other members of society, through tax-supported financial aid programs) help meet those costs, the IDEA proposal will do that. I don't think the Congress should have this goal.

Before closing, I want to make one final point about the income-contingency feature of the IDEA proposal. The data in Table 4 can be used to advantage here. The proposal requires the Secretary of Education to provide the various repayment options to the borrowers. It is very difficult to estimate the future earning of college graduates. If the Secretary allows borrowers to use 3 percent and 5 percent of earnings repayment schedules, and they earn very little, say $9,750 or less per year or perhaps earn nothing at all in many years, then the borrowers will not repay their loans in full. If they don't repay their loans in full, the government's costs for the program will rise precipitously. That being the case, the Secretary would be wise to ask all borrowers to repay their loans on a 7 percent of annual earnings repayment schedule. And if this is done, the income-contingency feature of the IDEA proposal is basically lost. Self-Reliance Loans, therefore, will not be "income-dependent" and the proposal will have been inappropriately named as well as ill-conceived.

Thank you for your attention to these remarks. I will be pleased to try to answer any questions you might have for me.

Table 1—Average Cumulative Stafford Indebtedness For Pennsylvania Baccalaureate Graduates of Four-Year Colleges, Average Annual Costs, and Loans As a Percent of Costs, FFY 1987 to FFY 1991

Four-Year Public Colleges

Year	Avg loan	Percent change	Avg Cost	Percent Change	Avg loan/cumulative 4-yr avg. costs
1987	$7,454	—	$6,895	—	29.3%
1988	7,769	+ 4.2%	7,265	+ 5.4%	28.9
1989	8,506	+ 3.5	7,895	+ 8.7	30.1
1990	9,150	+ 7.6	8,370	+ 6.0	29.7
1991	9,478	+ 3.6	9,235	+ 10.3	29.7
1987–1991	+$2,024	+ 27.2%	+$2,340	+33.9%	+ 0.4%

Four-Year Private Colleges

Year	Avg. loan	Percent change	Avg. Cost	Percent Change	Avg loan/cumulative 4-yr avg costs
1987	$8,062	—	$13,150	—	17.1%
1988	8,337	+ 3.4%	14,320	+ 8.9%	16.4
1989	9,232	+ 10.7	14,865	+ 3.8	17.0
1990	9,875	+ 7.0	16,055	+ 8.0	16.9
1991	10,154	+ 2.8	17,505	+ 9.0	16.1
1987–1991	+$2,092	+25.9%	+$4,355	+33.1%	-1.0%

Table 2—1989 Total Money Earnings of Persons With Four Years of College Education, By Gender and Race, Ages 25 to 34

	All Males	All Females	Total	White Males	White Females	Black Males	Black Females
Without Earnings	2.4%	10.9%	6.8%	1.6%	10.7%	5.7%	4.3%
Under $12,500	11.4	20.8	16.2	10.4	20.6	24.3	24.2
$12,500–$17,499	6.5	11.0	8.8	6.4	10.7	4.4	13.0
$17,500–$22,499	13.7	16.4	15.1	13.1	17.1	24.3	15.6
$22,500–$24,999	5.9	6.3	6.1	5.9	6.1	6.9	10.5
$25,000–$29,999	13.4	12.2	12.8	13.5	11.8	23.5	14.4
$30,000–$39,999	21.7	14.6	18.0	22.6	15.2	4.4	10.8
$40,000–$49,999	12.2	5.0	8.5	12.9	5.0	1.6	4.7
$50,000 or Above	12.8	2.8	7.7	13.6	2.8	4.9	2.5
All Earnings	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Avg. Earning	$32,465	$22,247	$27,216	$33,251	$22,277	$23,280	$21,646
Pct. in Group	48.6%	51.4%	100.0%	42.5%	44.6%	3.6%	4.0%

Source U S Bureau of the Census, Current Population Reports, Series P–60, No 172, Money Income of Households, Families and Persons in the United States 1988 and 1989

Table 3—Estimated Proportions of Four-Year College Graduates Ages 25 to 34 Who in 1989 Would Have Had Debt Burdens in Repaying Stafford Loans, by Cumulative Loan Amounts

Amounts borrowed	All Males	All Females	Total	White Males	White Females	Black Males	Black Females
$5,000	6.2%	20.3%	13.4%	4.8%	20.3%	15.4%	11.9%
$7,500	9.3	24.8	17.2	7.8	24.9	21.5	17.7
$10,000	13.8	31.7	23.0	12.0	31.3	30.0	28.5
$12,500	17.4	37.7	27.8	15.6	37.0	32.8	37.5
$15,000	23.0	45.6	34.6	20.6	45.1	40.9	42.6
$17,250	31.5	56.1	44.2	29.1	56.0	54.3	54.0

Percentages of All Borrowers With Burdens

Amounts borrowed	All Males	All Females	Total	White Males	White Females	Black Males	Black Females
$5,000	22.4%	77.6%	100.0%	15.4%	67.5%	4.1%	3.5%
$7,500	26.[illegible]	73.6	100.0	19.2	64.3	4.4	4.1
$10,000	29	70.8	100.0	22.1	60.8	4.6	4.9
$12,500	30.	69.6	100.0	23.8	59.1	4.2	5.4
$15,000	32.3	67.7	100.0	25.7	58.1	4.2	4.9
$17,250	34.7	65.2	100.0	28.0	56.5	4.4	4.9
All Grads	48.6%	51.4%	100.0%	42.5%	44.6%	3.6%	4.0%

Table 4—Comparison of Borrower Repayment Costs for $10,000 in Self-Reliance Loans at Three Proportions of Salaries and Four Initial Salary Levels

	$9,750 Per Year		$13,000 Per Year		$26,000 Per Year		$36,000 Per Year	
	Borrower Pays	Govt Forgives	Borrower Pays	Govt Forgives	Borrower Pays	Govt Forgives	Borrower Pays	Govt Forgives
3 Percent	$13,956	$23,281	$21,019	$ 0	$18,468	$ 0	$17,716	$ 0
5 Percent	$23,262	$ 5,622	$18,346	$ 0	$16,098	$ 0	$14,716	$ 0
7 Percent	$20,243	$ 0	$16,764	$ 0	$14,554	$ 0	$14,306	$ 0

Note Borrowers' initial salaries all assured to increase at 5 percent per year

Senator SIMON. Thank you.

Mr. Bigelow.

Mr. BIGELOW. Thank you, Senator Simon.

My name is Michael S. Bigelow, and I am deputy assistant commissioner for returns processing at the Internal Revenue Service. I appreciate the opportunity to testify today on the IRS views of the Self-Reliance Loan Act. I regret that we have not done an in-depth analysis of this bill as revised, and we just become aware of this hearing yesterday afternoon. However, we have reviewed similar proposals, and I will comment on concerns we see at this early stage.

With me today on my left is Jim Helm, the deputy assistant commissioner for collection.

I will keep my remarks brief but ask that my prepared statement be entered into the record.

Senator SIMON. It will be entered in the record.

Mr. BIGELOW. Right now, we are working with the Department of Education to examine the issues of mutual concern raised by this bill and similar bills introduced in the House. By raising concerns, we do not mean to convey a judgment on our part that these problems are insurmountable.

I also will not comment on the policy; however, I must point out that this proposal to have the IRS collect student loan repayments as a tax would be a fundamental change in the mission of the Internal Revenue Service and our role in the lives of taxpayers.

Before I comment on the legislation, I would like to give you a little background on the size and scope of IRS operations today.

The Internal Revenue Service affects the lives of almost all Americans. During 1991, the Internal Revenue Service processed more than 200 million tax returns and more than one billion infor-

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mation returns, sent out refunds to more than 80 million taxpayers and collected more than $1 trillion.

The IRS has a longstanding commitment to making the tax system simpler and more responsive to the needs of taxpayers. Because even a minor change can have a substantial impact on the overall tax administration system, it is important to carefully consider any changes that could affect our ability to collect the more than $1 trillion owed the Government each year.

In analyzing any new proposal, we must consider its impact on taxpayer burden and complexity. The IRS already collects delinquent nontax debts owed the Federal Government. Our refund offset program has been successful in securing past due Federal debts. In 1991, IRS offset over 1.5 million refunds and secured over $900 million for all Federal agencies. Of that amount, over $360 million for defaulted student loans was remitted to the Department of Education.

Taking into account all of these factors, Congress and the administration must ultimately make the policy decision whether the IRS should move from our role as debt collector of last resort to establishing the tax system as the primary collection vehicle for student loans.

Above and beyond the policy decision of whether IRS should become the Government collector for Federal debts, we have some very practical concerns about the feasibility of such a proposal. These reservations stem from an analysis of the impact of the self-reliance loan proposal on the ability of taxpayers and employers to cope with the changes, the current tax processing limitations, our revenue accounting systems, and our tax collection activities. Moreover, we currently have neither the computer capacity nor the resources to undertake such an effort at this time.

The bill envisions that the student's loan payments would be paid along with his or her current year's tax. To do this effectively, we anticipate altering the withholding tables and estimated tax worksheets, as was previously described, to ensure that taxpayers pay in the amounts that would be due for student loans.

The self-reliance loan proposal would have a significant impact on the Service's current processing systems. Implementing the provisions would require substantial forms and processing changes, increased capacity, new accounting routines, and increased collection enforcement resources.

Former Commissioner Goldberg and other IRS executives testified last year before both Houses of Congress about our need to modernize our tax system. We are at a crossroads at the IRS. Outmoded systems designed in the 1960's make it difficult for us to properly store, timely deliver or update information already in our system. If the IRS is to be charged with a new area of taxation, we would need to begin planning for this as part of our tax system modernization effort now underway.

To implement this legislation, the Form 1040 would have to be revised to report the educational loan repayment tax and to record loan payments transmitted. Adding a new line and schedule to the Form 1040 is much easier said than done. We would have to adapt our accounting system to establish a new trust fund and to process self-reliance loan transactions. At first glance, we would need to report to the Office of Self-Reliance Loans information similar to what we now report to the Social Security Administration for Social Security and Medicare taxes.

As we contemplate processing changes for 1993 and beyond, we are confronting very real limits to our ability to capture information from the Form 1040. There would also be a tremendous impact on taxpayer service sites and service centers responding to inquiries about repayment status, deferral rules, and other aspects of the program each year during our busiest tax season.

Senator Coats articulated our concerns as to collection impact. The collection of delinquent student loan repayment taxes could add to the very sizable existing accounts receivable inventory, which unfortunately includes a sizable trust fund portion from employers.

We are concerned that loan repayment taxes could be assessed as early as tax year 1993. We would need significant coordination with the Department of Education and the Census Bureau to develop protocols for ongoing information needs. Even a 4-year demonstration project may be too short to determine the total impact on the Internal Revenue Service because repayments for the majority of students would not begin until the project really is over.

From our preliminary analysis, start-up costs for the Internal Revenue Service would be significant. And Mr. Chairman, I do not want to convey the impression that the Internal Revenue Service would not be able to collect the educational loan repayment tax if that is the will of the Congress and the President. We know that with proper planning, we can implement major tax legislation. We have done so in the past, and we expect to make major changes in the very near future.

As I noted at the beginning of my statement, we will continue to work with the Department of Education to pursue these issues in greater detail and in a variety of scenarios.

We appreciate your taking this opportunity to determine what the impact on the IRS would be as you consider this legislation. Mr. Helm and I will be pleased to answer any question you or the members may have.

[The prepared statement of Mr. Bigelow follows:]

PREPARED STATEMENT OF MR. BIGELOW

Mr. Chairman and Members of the Committee: I appreciate the opportunity to testify today on the IRS' views on the Self-reliance Scholarship Act of 1991. I regret that we have not done an in-depth analysis of this bill, however, we have reviewed similar proposals and I will comment on those concerns we see at this stage of our inquiry. With me today is Jim Helm, the Deputy Assistant Commissioner for Collection.

OVERVIEW

We are working with the Department of Education to examine the issues of mutual concern raised by this bill and similar bills introduced in the House. By raising these concerns, we do not mean to convey a judgment on our part that these problems are insurmountable.

I also will not comment on the policy, however, I must point out that this proposal to have the IRS collect student loan I also will not comment on the policy, however, I must point out that this proposal to have the IRS collect student loan repayments as a tax would be a fundamental change in the mission of the IRS and our role in the lives of taxpayers.

SIZE AND SCOPE OF IRS OPERATIONS

Before I comment on the legislation, I would like to give you a little background on the size and scope of IRS operations. The Internal Revenue Service affects the lives of almost all Americans. Our taxpayer base includes all individuals, families, businesses, trusts, estates, tax exempt organizations, and government agencies throughout the United States, and others throughout the world who do business in the United States. Our budget for FY 1992 is almost $6.7 billion and we have over 115,000 employees in our service centers, call sites, district offices and overseas posts of duty.

During 1991, the IRS processed more than 200 million tax returns and more than 1 billion information returns, sent out refunds to more than 80 million taxpayers, and collected more than 1 trillion dollars. We sent out more than 8 million notices to taxpayers who made math errors, or forgot to sign or attach schedules to their returns; sent out more than 2 million notices requesting name and Social Security Number and received more than 40 million letters in our service centers. We handled more than 36 million calls in our Taxpayer Service call sites and received more than 3.6 million calls and placed more than 3.2 million calls in our Collection Automated Call Sites.

We enforced compliance with the tax laws by conducting more than 1 million examinations and sent out more than 4 million notices to taxpayers who did not include all of their income on their returns. We also sent out more than 18 million balance-due collection notices and initiated more than 4 million collection actions (ranging from filing notices of tax lien to bank levies and property seizures).

To support all of these activities, IRS employees requested copies of more than 40 million tax returns from archives for our use, and received more than 6 million requests from taxpayers for copies of their returns. We made more than 54 million inquiries to our master files and effected more than 700 million transactions to master file accounts.

THE NEED FOR TAX SIMPLIFICATION

The IRS has a longstanding commitment to making the tax system simpler and more responsive to the needs of taxpayers. Because even minor changes can have a substantial impact on the overall tax administration system, it is important to carefully consider any changes that could affect our ability to collect the more than one trillion dollars owed the government each year.

In analyzing any new proposal, we must consider its impact on taxpayer burden and complexity.

COLLECTION OF NON-TAX DEBTS BY IRS

The IRS already collects delinquent non-tax debts owed the federal government. Congress first authorized the collection of delinquent child and spousal support payments through offset of taxpayers' refunds in 1981. Refund offset was expanded in 1984 to other federal non-tax debts, such as unpaid student or small business loans.

The refund offset program has been successful in securing past due federal debts. In 1991, IRS offset over 1.5 million refunds and secured over $900 million for all federal agencies. Of that amount, over $360 million for defaulted student loans was remitted to the Department of Education.

Taking into account all of these factors, Congress and the Administration must ultimately make the policy decision whether the IRS should move from our role as debt collector of last resort to establishing the tax system as the primary collection vehicle for student loans.

Above and beyond the policy decision of whether IRS should become the government collector for all federal debts, we have some very practical concerns about the feasibility of Such a proposal.

These reservations stem from an analysis of the impact of the Self Reliance Scholarship proposal on 1) the ability of taxpayers and employers to cope with the changes, 2) the current tax processing system limitations, 3) our revenue accounting system, and, 4) our tax collection activities. Moreover, we currently have neither the computer capacity nor the resources to undertake such an effort.

IMPACT ON TAXPAYERS AND EMPLOYERS

The bill envisions that the student's loan payments would be paid along with his or her current year's tax. To do this effectively, we anticipate altering the withholding tables and estimated tax worksheets to ensure that taxpayers pay in the amounts that would be due for student loans. It is critical that you allow sufficient lead time to develop educational materials for taxpayers and employers.

The IRS takes very seriously its role in educating taxpayers about the best way to meet their tax obligations. In order to avoid a large number of taxpayers discovering that they owe a significant amount and must pay it within a short time, the Form W-4 (Employee's Withholding Allowance Certificate) would have to be revised to factor loan repayments into the withholding calculation. Although this would further complicate the Form W-4, which already contains a page of additional worksheets for taxpayers with two jobs or for two wage-earner households, we believe it would be necessary to avoid balance due tax returns.

IMPACT ON IRS PROCESSING AND ACCOUNTING SYSTEMS

The Self-Reliance Scholarship proposal would have a significant impact on the service's current processing systems. Implementing the provisions would require substantial forms and processing changes, increased capacity, new accounting routines and increased collection enforcement resources.

Former Commissioner Goldberg and other IRS executives testified last year before both Houses of Congress about the need to modernize our tax system. We are at a crossroads at the IRS. Outmoded systems make it difficult for us to properly store, timely deliver or update information already in our system. If the IRS is to be charged with new areas of taxation, we would need to begin planning for this as part of Tax Systems Modernization.

To implement this legislation, the Form 1040 would have to be revised to report the Educational loan repayment tax and to record loan payments transmitted. Adding a new line and schedule to the 1040 is much easier said than done. At a minimum, we would need to work closely with the new Office of Self-Reliance Scholarships to ensure that their notice and our Schedule are compatible and do not cause undue taxpayer confusion.

The IRS would have to adapt our accounting systems to process Self-Reliance Scholarship transactions. At first glance, we would need to report to the Office of Self-Reliance Scholarships information similar to what we now report to the Social Security Administration for Social Security and Medicare taxes.

As we contemplate processing changes for 1993 and beyond that we know about, we are confronting very real limits to our ability to capture information from the Form 1040. Modifying the computer record that is built from the Form 1040 to transmit information to the Individual Master File to accommodate loan repayment tax information would require format changes which would create unacceptable overhead severely impacting processing times.

There would also be a tremendous impact on taxpayer service sites and service centers responding to inquiries about repayment status, deferral rules and other aspects of the program each year during our busiest season.

IMPACT ON COLLECTION ACTIVITIES

In addition to the processing issues, which are significant, additional workload would be incurred in our Collection function. The collection of delinquent student loan repayment taxes could add to the very sizable existing accounts receivable inventory.

We have a major effort underway to improve our handling of accounts receivable which has been the subject of numerous hearings before Congress over the last two years. We appointed a high level executive to serve as Accounts Receivable Executive Officer. This executive is responsible for coordinating the many different aspects and IRS functions that must work together to reduce the rate of growth in accounts receivable, particularly in uncollectible accounts.

LEAD TIME AND RESOURCE NEEDS

We are concerned that loan repayment taxes could be assessed as early as tax year 1993. We would need significant coordination with the Department of Education and the Census Bureau to develop protocols for ongoing information needs. Education, for example, is responsible for determining the eligibility of an institution to participate in the loan program. We would also have to coordinate systems modification efforts with the Office of Self-Reliance Scholarships.

We have not estimated either the cost of modifying our systems or the operational costs once implemented. Significant coordination also would be necessary to develop common assumptions that would enable all IRS functions to accurately estimate the time and resources necessary to implement this bill. From our preliminary analysis, start-up costs would be significant. Since the bill allows for administrative costs to be paid from the Education Trust Fund, we assume that we could work with the Finance and Appropriations Committees to determine a formula for reimbursement of start-up and ongoing expenses.

CONCLUSION

Mr. Chairman, I do not want to convey the impression that the IRS would not be able to collect the Educational Loan Repayment Tax if that is the will of the Congress and the President. However, I must emphasize that this would be a major change in the way we do business and would impact many different aspects of our tax administration system.

We know that, with proper planning, we can implement major tax legislation. We have done so in the past and we expect to make major changes in the very near future. As I noted at the beginning of my statement, we will continue to work with the Department of Education to pursue these issues in greater detail in a variety of scenarios.

We appreciate your taking this opportunity to determine what the impacts on the IRS would be as you consider this legislation.

Mr. Helm and I will be pleased to answer any questions you or the members may have.

Senator SIMON. We thank you.

Ms. LaFever, if we make 300 schools eligible for this, I gather the University of Phoenix will not be one of the 300 applying. Is that correct?

Ms. LAFEVER. The way it is currently set up now, I do not believe so. But since you brought up the area of 300 schools, I would like to make a couple points.

If you have 300 schools, or even a smaller number, you could endanger access to education for other institutions within a given State because right now, in order for a lender to make additional loans, they have to sell those loans to a secondary market, the original loans, to get additional money. When they sell them to secondary markets, in order for that market to have the funds to purchase additional loans, they have to go through bonding.

A bonding agency for the last couple of years has been requiring a portfolio mix because of the high default rates that some institutions have had. That portfolio mix is normally a small percentage of proprietary, a small percentage of 2-year institutions, and the largest percentage, because of their lower default rate, is for 4-year institutions.

For example, in the State of Arizona, we have one of the largest 4-year institutions in that State. If they chose to go to this program and to not make the same number of loans out of the Guaranteed Student Loan program that they are, they could endanger access to the rest of us to additional funding under that Guaranteed Student Loan program. That scares me.

Another——

Senator SIMON. I don't mean to cut you off, but we have both Republican and Democratic Caucus meetings. I think those kinds of problems can be taken care of, but specifically answering my question, then, you would not be applying as one of the 300.

Ms. LAFEVER. Not the way it is currently designed.

Senator SIMON. OK. Mr. Davis, when you stress that the total payment is going to be greater, it is true if you have a 20-year mortgage, you're going to pay a greater amount than if you have a 10-year mortgage. I think people understand that if you pay something back over a longer period of time you pay more interest. But sometimes it is not possible for families to make large enough payments to pay back in 10 years like they can in 20 years.

If I may ask this question of you, Mr. Bigelow or your colleague, how does the child support program work right now?

Mr. BIGELOW. Right now, they have a refund offset for child support. We have created what we call a debtor master file, and we receive information every year from all of the various States on back child support. We load that into the file, and as returns are filed for a refund, we run in past that particular file and offset any back due or delinquent child support. We have the same thing for default student loans.

Senator SIMON. I see. But that would be appreciably different, then, from this kind of an operation. Here, you would probably have to have, particularly if we went beyond the 300 schools, clearly some kind of modification of the W-2 Form.

Mr. BIGELOW. We'd have to have a modification of the W-2, we'd have to have a modification of the 1040, an additional line to report that and possibly a schedule, but more importantly, an entire new accounting technique set up in order to capture that and be able to properly report it to whatever body is established to receive that.

Senator SIMON. Senator Kassebaum.

Senator KASSEBAUM. Thank you.

First, I would like to thank everybody who is here testifying. I know it was not easy to make arrangements at the last minute. We didn't know about this hearing until the weekend. I think you probably weren't even asked until Monday, as everyone was scrambling to get witnesses. So I very much appreciate your testimony, and of course, I think it makes eminent good sense. I think it shows just by the questions, Ms. LaFever, that you raise here that we all need to be sure we are comfortable with how this is going to work before we can move forward. I think there are just many unanswered questions, and many that all three of you have raised.

Mr. Bigelow, I would like to follow up on the child support question. Is that interstate coordination that you meant? How do you track that?

Mr. BIGELOW. Yes, it is interstate coordination. We have worked out memoranda of agreement with each of the various States. We do have a few States that do not participate, but the majority do.

We also have the same thing for approximately 28 Government agencies in order to secure refunds on back taxes and Federal obligations.

Senator KASSEBAUM. Let me just ask if the collection of these loan were run through the IRS, would you have to initiate a new computer system, or could you do it with the one that you have?

Mr. BIGELOW. We would have to add additional accounting routines, which is a very complicated technique, to capture and record the information so that we know exactly how to distribute the funds. It doesn't just all go into the Treasury; it has to be accounted for. It is that routine that would have to be run that would increase our processing time in Martinsburg on our antiquated systems which, like I said, were designed in the 1960's. The estimated lead time is a couple of years just to build that in, and additional capacity would have to purchased, and you know the procurement process.

Senator KASSEBAUM. Do you have any rough estimate of what the might be? I guess that's probably open-ended.

Mr. BIGELOW. We really have not. We have been working with some of the staff on the House side in trying to determine some of the costs, because a lot of it depends on how you actually build this as far as is this a tax, and add it to the tax system with a trust account, or is it kind of like an add-on, supplemental to tax, which is some of those proposals on the House side. So it depends on how it's built and what resources we would need, so we would have to work with the staff. We are trying to work with the Department of Education right now in determining some of these costs.

Senator KASSEBAUM. Mr. Davis, we have worked hard, as you know, to develop some integrity measures that are based on the default rates. This has been criticized by some schools which have faced closure and which, with patterns of high default rates, have simply not been able to succeed.

What would this proposal do to those efforts to try to strengthen program integrity? Have you given any thought to that?

Mr. DAVIS. Do you mean this particular program?

Senator KASSEBAUM. Yes, because there would be no institutional default rates.

Mr. DAVIS. No, I would doubt that those schools that have high default rates would even be selected by the Secretary, so I don't think it would have any——

Senator KASSEBAUM. True, but now we're speaking about just the 300 schools. If this program grows, which I guess it would, it would be open-ended. Possibly, no institution would have a default rate.

Mr. DAVIS. Yes. It would represent a raid on the Treasury by such schools. But I would like to think that by the time this is ever implemented—and I hope it isn't, but say it is implemented—5 years from now, I would like to think that most of the schools that are not performing to standard will no longer be in any of the programs. I have that as a hope, anyway. We're working on it in Pennsylvania.

Senator KASSEBAUM. Well, I salute that, because I think that's what it will take. I value that contribution.

Ms. LaFever, the University of Phoenix is a proprietary school. Do you see the absence of a default rate measure as being a problem?

Ms. LAFEVER. Yes, being a proprietary institution with a 1.8-percent default rate, by the way——

Senator KASSEBAUM. I know; you are an example of one that is well-run.

Ms. LAFEVER. We even find ourselves starting to become just a tad defensive, because everyone considers proprietary schools to be bad institutions in this day and age. In the State of Arizona, we have been able to close 12 schools in the last year, institutions that were perhaps not using the best systems in order to implement their financial aid programs. The way that has taken place is through the State licensing agency and the guarantee agency working hand-in-hand in identifying institutions that have problem areas, and if those institutions cannot be helped, then they step in and take the actions that are needed.

So I think the mechanism is already in place.

Senator KASSEBAUM. Based on the ability to use the default rate as a measure of whether they should continue or not, have you used that as a guideline?

Ms. LAFEVER. What happens right now is the guarantee agency requires any institution with a high default rate to fill out a very extensive questionnaire—it takes about a week—and based on that, they determine whether that institution should be allowed to continue participation in the current Guaranteed Student Loan program. So they do use that as a basis.

Senator KASSEBAUM. I don't have any further questions. I think your comments regarding the questions that need to be answered and need to be thought through before we put anything in place are extremely valuable, and I am very appreciative of your time in coming to testify.

Senator SIMON. We thank you all. I think this is evolving, and we still have things to work out. It sounds to me like IRS needs help no matter what, whether we pass this or not.

Mr. BIGELOW. We need help with our tax system modernization.

[Additional statements and material submitted for the record follow:]

PREPARED STATEMENT OF THE UNITED STATES STUDENT ASSOCIATION (USSA)

The United States Student Association (USSA), the largest and oldest national student organization, represents more than 3.5 million postsecondary students in 4-year public and private institutions, technical schools and community colleges. USSA applauds the Senate for its passage of S. 1150, "The Higher Education Act Amendments of 1992," which would go a long way toward our shared goal of equal educational opportunity. We are disappointed that this important legislation did not include a Pell Grant entitlement. which we believe is a necessary prerequisite for making higher education accessible to all.

Basically, the USSA Board of Directors appreciates the intent of Senators Simon, Durenberger, and Bradley to help students and their families afford a postsecondary education, and to lessen the impact of post-graduation debt burdens. However, USSA is concerned about some aspects of these two bills, including student loan collection through the Internal Revenue Service; 25-year repayment periods; and elimination of the in-school interest subsidy. We thus have some thoughts on how income-sensitive loan repayment as an option could be used in the interests of students.

Let me emphasize that USSA is a strong supporter of the concept of the direct lending of student loans by institutions. While we have many concerns regarding how a direct lending system would be phased-in and executed, we are very supportive of the concept because of the enormous savings and enhanced simplicity of such a system. This testimony will also detail these concerns. Let me finally emphasize that USSA sees the issue of direct lending as very separate from S. 1845 and S. 1562's provisions for income-contingent loan repayment through the IRS.

Lastly, USSA recognizes that the student loan programs have enabled countless students to pursue a postsecondary education. However, our recommendations for the student loan programs and repayment options are accompanied by our strong belief that a Pell Grant entitlement is a necessary prerequisite to making our loan programs work in the interests of students

INCOME-CONTINGENT LOAN REPAYMENT

USSA agrees with Senators Simon, Durenberger, and Bradley that income-sensitive loan repayment is an idea well worth considering. It is true that students are graduating with huge and often onerous loan burdens: in 1986, students graduated from public institutions with an average debt of $6,810 and from private schools with an average of $10,000 worth of debt. That is why we are supportive of a number of provisions in the House Reauthorization bill (H.R. 3553), which would ease the loan burden from students, including provisions to:

—Provide graduated repayment schedules for Stafford Loan borrowers who request it [Section 424 (a)];

—Requires that students be notified by both the seller and the purchaser when their loan is sold [Section 427 (i)];
—Mandate that graduated or income-sensitive repayment schedules be offered to consolidation loan borrowers [Section 430 (f)].

S. 1845 and S. 1562 both involve income-contingent loan repayment through the Internal Revenue Service, and the direct lending of loans through institutions. Both create unsubsidized loans, and S. 1845 would eliminate the current student loan programs and replace them with IDEA credit assistance. In an attempt to make the loan repayment process more manageable for students and to decrease the number of student loan defaults, students would pay their loans (under the two new programs) on an income-contingent basis through increased payroll-tax withholding.

S. 1845 (THE INCOME-DEPENDENT EDUCATIONAL ASSISTANCE)

While USSA does support the idea of income-sensitive methods of loan repayment, we would be concerned about S. 1845's construction of income-dependent loan assistance for the following reasons.

(1) S. 1845 would exacerbate the loan/grant imbalance, particularly among dependent students. S. 1845 would replace the Stafford and Supplemental Loans for Students (SLS) with IDEA credit. Currently, independent students (and in exceptional circumstances, some dependent students) are eligible for SLS. For students not eligible for SLS, S. 1845 increases the maximum loan limits under IDEA by $3,975 to $4,000, but only increases the maximum Pell Grant by a $600 "entitlement." S. 1845 would thus increase these students' dependence on loans.

However, independent (and other) students currently eligible for Stafford and SLS loans would see a decline in the loan amounts they can borrow (between $125 and $500)—which USSA finds objectionable in light on skyrocketing college costs.

Annual Loan Limits

Undergradute	Current Staffod	Current SLS	S 1845 IDEA Credit	Difference
1st and 2nd Year Dependent Students [1]	$2,625	—	$6,500	$3,975
1st and 2nd Year Independent Students	$2.625	$4,000	$6.500	- $125
Other Dependent Undergraduates [1]	$4,000		$8,000	$4,000
Other Independent Undergraduates	$4,000	$4.000	$8.000	$ 0
Graduate/Professional [2]	$7,500	$4,000	$11,000	- $500

[1] The PLUS loan program for parents of dependent students would continue under S 1845

[2] Under S 1845, medical and other high-cost doctoral degree students would be eligible for up to $20,000 of IDEA credit Students in extraordinarily high-cost graduate degree programs would be eligible for up to $30,000.

(2) Under H.R. 2336, the interest rate on IDEA would float (T-bill plus 2 percentage points, not to exceed 10 percent) and have no in-school interest subsidy; this would make IDEA loans much more onerous for needy students. IDEA loans would also have no origination fees and insurance premiums. USSA is not convinced that these factors "cancel each other out." In fact, Mr. Simon's own statistical analysis indicate that many students would see an increase in their total student loan indebtedness after graduation if they chose IDEA loans over Stafford loans. Students in long-term programs and graduate school would generate particularly huge IDEA loans. We believe that it is the responsibility and in the self-interest of the federal government to offer student loans with manageable terms and that will have the least impact possible on the job and career choices of graduates. Hence if students must borrow to finance their postsecondary education, the loans they take out should only be Perkins and Stafford Loans, which have subsidized interest rates and an in-school interest subsidy.

We only have to look at the current SLS program to see the adverse affects of a loan program lacking an in-school interest subsidy. Looking at an actual Repayment Addendum and Disclosure Statement from a lender to a SLS borrower, a student from Louisiana, shows that after she makes repayments on her SLS loan of $4,000 over the next nine years, she will have had to repay $8,362. She will have to pay $8,362 for a $4,000 loan. It's crazy that poor people are expected to pay twice as much for their education!

Now, S. 1845 attempts to address the problem under the current Income Contingent Loan program of students forever paying off their loans because of negative amortization—that is, students whose low-paying jobs result in their paying off the interest but never touching the principal, and remaining indebted for life—by forgiving their IDEA loan after 25 years of repayment. 25 years is a long time to keep penalizing students, and is hardly a reward for taking out an ever-growing loan. The indisputable bottom line is that if you are on a 25-year loan repayment plan, you end up paying much more than if you were on the standard 10-year plan. Under such a prolonged repayment period, borrowers would still be paying off their loans while in their 40's and 50's, and when many are trying to purchase homes and raise families. In any event, USSA believes that it must be a conscious choice for students to commit themselves to such a prolonged repayment period that means ultimately that they owe a huge amount to the federal government and end up repaying quite a lot of money.

(3) S. 1845 may complicate, not simplify, the student loan repayment process. While USSA strongly supports the idea of income-sensitive loan repayments as a more fair and manageable way for students to repay their loans, we have concerns about S. 1845's particular way of collecting income-dependent loan repayments through the IRS.

—*Where are students supposed to turn to for counseling and information on their student loan repayment options and problems?* The IRS? The current system is far from perfect, but at least students can work with their lender on deferment and forbearance options. Will the IRS or the Department of Education provide counseling?

—*What if a student is drawing a salary but is in economic trouble?* We fear that it would be nearly impossible for students to negotiate their loan payments with the IRS, and instead the agency would simply continue to take precious dollars from young peoples' paychecks (and then their house, their car . . .).

—*What happens if the Department of Education (or whichever entity is keeping track of what students owe) makes a mistake?* If the department erroneously assumes that a student still owes money, what is his or her recourse?

—*How can students predict what their monthly loan payments will be?* After graduation, a student's earnings are probably the most unpredictable aspect of his/her life! Won't employers have increased administrative expenses as participants in loan collections?

USSA also believes that students should consciously and freely choose—upon beginning repayment—a 25-year income-contingent loan repayment schedule that will increase the total amount they pay back, and the years they are struggling to make payments. They should NOT automatically be tracked into a 25-year payment agreement.

S. 1562 (SELF-RELIANCE SCHOLARSHIPS)

Our concerns about S. 1562 are very similar to those we have regarding S. 1845. S. 1562 would allow students to borrow up to $10,000 with a maximum of $33,000. Borrowers could choose among 15, 20 or 25 year repayment options. The exact impact of these different options for borrowers is not clear to us. In addition, under S. 1562 a minimum level of repayment is set so a borrower could not avoid repaying their loan even if they are unemployed. While this avoids the problem of a disincentive to work, it could impose real hardships for students, many of whom—in today's tough economic times—are finding it difficult to obtain steady and well-paying jobs. We do appreciate the fact that the Self-Reliance Scholarships would supplement and not replace current loan programs.

One last concern is that both these bills would provide quite an incentive for institutions to raise tuition. Schools could continue raising tuition, which would be matched dollar-for-dollar by increased loans for students (to a high level because both would, overall, increase maximum loan limits). Pell Grants, however, would not increase dollar-for-dollar as tuitions rise.

USSA also has some philosophical problems with the premises behind these two bills that proposes to create new loan programs to address the very real problems of declining access to higher education, skyrocketing college costs, and difficult student loan burdens. New loan programs will not sufficiently address the underlying reason why students default on their student loans. We should not assume that all of these students choose not to pay back their loans; we should recognize that most of them simply can't pay them back. While USSA shares the concern about the increasing costs of Stafford Loan defaults, we believe that better loan collection through the Internal Revenue Service is not the answer. What is desperately needed is an in creased commitment to retention programs and grant programs, including a Pell Grant entitlement.

There are many reasons why students default, including ones for which it is unfair to assign blame to the student.*Half of Stafford Loan defaulters are dropouts from postsecondary programs.* These people are not likely to have the job prospects or enhanced earning power that accompany a postsecondary degree or certificate, and thus face difficulty repaying their loans. Many student loan defaulters WANT to pay back their loans; they just CANNOT. Hence, we must strengthen our investment in the retention programs—including the TRIO Programs for Students from Disadvantaged Backgrounds—that enable students to stay in school. We must make Pell Grants an entitlement . . . which would decrease the amount of low-income students forced to take on huge loans to pay for their postsecondary education and increase their persistence rates. We must also ensure that students have all the knowledge necessary to make good decisions and to be responsible and informed student loan borrowers—and S. 1150 would definitely help in this area. Without these changes, better loan collection techniques through the IRS will not help improve the number of students paying back their loans.

INCOME-CONTINGENT LOAN REPAYMENT FOR STUDENTS WITH ECONOMIC HARDSHIP

USSA agrees with the proposal advanced by the American Council on Education on income-contingent loan repayment for borrowers whose income is inadequate to service their debt for a period of years (i.e. those who debt service exceeds 10 percent of their income). This group includes students who choose a career in low-paying public interest fields, as well as those who did not persist in higher education and do not have significantly higher incomes. We join ACE in believing that these borrowers should have the option to petition the government to allow them to repay on an income-contingent basis during the period in which their salaries are inadequate to service their debt without great hardship. Interest during this period that is not taken care of by the borrowers' payments should be forgiven and not added to their total debt. For most borrowers, this period of lower payments would probably be temporary, but for those who are still repaying their loan after a certain period of time (25 years or so) should have their remaining debt forgiving.

We believe that this kind of optional income-contingent loan repayment takes care of many of our concerns regarding most income-contingent proposals. Students would not just automatically be put on the 25-year loan repayment track: since they would have to petition for such a payment plan, they would be fully cognizant of the implications of income-sensitive repayment (i.e. it could extend the number of years they would be paying off their loans).

We believe that this kind of income-contingent proposal is both feasible, necessary, and much more in the interests of students. Under these other proposals, USSA is concerned that students would simply fall into 25-year loan repayment plans without a conscious choice to do so and without an understanding of all the consequences. Many students do not get all the necessary information when they first receive and/or start repaying their loans. For many, taking out a loan is the very first financial decision in their lives. Students should not choose at the outset of receiving their loans a 25-year repayment period simply because they are anxious about their future income potential after college. In any event, an optional post-graduation income-contingent repayment process would be the student's choice. and not something into which he or she falls and later regrets.

Also, at this time, we are still uncomfortable about the Internal Revenue Service playing any role in student loan collection.

DIRECT LENDING

The second major element of these two bills are their use of federal borrowing as the source of loan capital for student loans. At USSA's 44th Annual National Student Congress held in August 1991, students from all over the country voted to support the concept of the direct lending of student loans by institutions, based on the following:

—*Simplification of the loan application, delivery, updating, and repayment processes . . . and reduction of loan defaults.* The current GSL structure of more than 13,000 lenders, over 50 guarantee agencies, and many secondary markets results in an overwhelming system of multiple application forms, fees, paperwork and massive confusion for too Many students. By contrast, the Perkins Loan program is far easier for students to understand and use. USSA believes that many defaults are the result of the complexity and confusion of this system that leaves too many students with too little information and no sense of who to go to for answers.

—*Increased efficiency.* Because of the complicated nature of the system, students experience numerous delays in getting their loans, causing much hardship: students are penalized for paying their tuition bills late or are dropped from their classes, and have difficulty paying their child care costs or putting food on the table. Under a direct loan program—like the Perkins Loan program—a school could process and deliver a loan along with a student's regular financial aid application. In addition to reducing paperwork, the school would have direct control over the timing and distribution of loan funds. Hence, students would receive their loans more promptly.

—The possible elimination of origination fees and insurance premiums.

—The possibility of substantial savings (a reduced need to pay the special allowance rate) that could be channeled into increased grant aid. Estimates of savings range from $600 million to $1.4 billion.

—Automatic loan consolidation.

—*Reduction in defaults/better counseling.* If schools originate the loans along with the regular financial aid application, students would get more and immediate information on how and when to repay their loans, and deferment and consolidation options. In addition, a Harvard study found that a direct loan program would reduce or simplify 44 percent of its administrative functions associated with the current Stafford Loan program. A decrease in the administrative complexity for institutions would mean that schools could devote more of their energies on reducing defaults through better counseling of student loan borrowers.

However, USSA hopes that the following questions will be satisfactorily answered as the Committee discusses and considers direct lending:

—Will there be adequate capital so that the loan program will remain an entitlement under which every student who is eligible for the program can get a loan?

—Will there be a phase-in period so that there is opportunity to assess and address problems in the system?

—How do we prevent institutions from "red-lining" students they consider risky borrowers? Since institutions are being held responsible for high default rates (i.e. high default schools are being cut off from participation in student loan programs), will they deny loans to students whom they think are likely to drop out and default? Will this end up denying first-generation college students, and students from low-income and ethnic minority backgrounds access to loans and a postsecondary education?

—If financial aid offices at direct lending institutions take on new overhead costs and thus require additional funding, will there be new costs passed on to students? Would direct lending really eliminate the need for origination fees and insurance premiums? If there are savings from restructuring the loan program, will they go to student aid programs? Or will all savings be lost to new administrative costs for the Department of Education and institutions?

—Will nontraditional students—older students, part-time students, and evening students—receive adequate services regarding loans if financial offices are only open during the day?

USSA looks forward to further discussing these issues as you consider direct lending proposals, and stands ready to be of assistance. We think that the direct lending could be a powerful way to ensure that student loans work in students' interests.

Lastly, USSA is aware that Senators Kennedy, Simon, Durenberger, Bradley and Bentsen have been engaged in discussions on a supplemental, demonstration project incorporating elements of S. 1845 and S. 1562. Attached is USSA's recommendations for what a pilot direct lending programs should consist of. However, a supplemental, demonstration project would answer some but not all of USSA's concerns regarding income-contingent loans with IRS collection. These include the absence of an in-school interest subsidy, a lack of choice over whether to engage in a 25-year payment period, and IRS collection. Lastly, it is of great concern to USSA that this represents an attempt to create a new loan entitlement for some needy students at the same time that the Senate chose not to find funding for a Pell Grant entitlement. It seems curious to us that the Senate failed to agree to a Pell Grant entitlement, whose merits are never questioned by critics—only the wisdom of creating another entitlement is brought up—yet is apparently eager to create yet another student loan entitlement. This is also unfortunate in light of the widely understood problem of the loan/grant imbalance.

In conclusion, USSA urges this Committee to carefully consider how any income-contingent loan program, and/or direct lending system would work and whether our shared goals of increased access, enhanced information and loan repayment rates, and simplification of the student loan system would be achieved.

[For more information, contact Selena Dong or Stacey Leyton at (202) 347-8772.]

ELEMENTS OF A PROPOSED DIRECT LOAN DEMONSTRATION

1. How long should the demonstration be conducted?

At least ten years would be necessary in order to fully assess the impact of all aspects of the proposed concept, including flexible and income-contingent repayment. The current income contingent loan demonstration would be terminated.

2. How many institutions should participate in a proposed demonstration?

The size of the demonstration is not nearly an important as achieving the proper representation of institutional participants and a cross-section of student borrowers from all income groups. While some have suggested 250 institutions and others 500, either is acceptable with two caveats: (a) the Congress should determine the representation of institutions in the sample, not the Secretary; and (b) the sample must be heavily weighted toward the categories of institutions whose capacity to administer a campus-based direct lending program is in doubt. Of critical importance to USSA, in addition, is the income mix of student borrowers to be included in the institutions selected. We suggest the following using either 250 or 500 institutions:

Student Borrowers

Institutions		Sector/No. of Students
250	500	
20	40	Public/Private Research
30	60	Smaller, Private, BA (1,500 students or less w/1,000 GSL borrowers)
30	60	Public, BA (4,000 students or less w/2,000 GSL borrowers)
30	60	Community, Junior and Vocational-Technical Colleges
10	20	Historically Black Colleges and Universities (HBCU's)
10	20	Urban, BA (5 public, 5 private)
10	80	Private career schools (mix of collegiate, degree-granting, technical with short-term programs, and cosmetology)
30	60	Selected by Ed to ensure geographic, within-state distribution and balance.

3. What should be the appropriate balance of student borrower/participants in the direct loan demonstration?

The student mix at each participating institutions must assure that the borrowing profile considers such student characteristics as family income, amount of the loan, student career objective and independent/dependent student status among others.

4. How will loan capital be provided to colleges and schools to deliver to students?

USSA is very concerned about the source of loan capital. Various direct loan proposals have suggested raising funds from the sale of T-bills, while others have suggested borrowing from the Federal Financing Bank (FFB). We are concerned about the implications of any mechanism that has the possibility of limiting the entitlement nature of the GSL program, i.e. providing controls in the Department of the Treasury, OMB or other governmental agency or office which could limit student access to GSL funds for college. We see signs that either of these mechanisms for providing GSL loan capital will provide an opportunity for "control" of the flow of capital to participating postsecondary institutions. Then control could limit student access and is likely to change the entitlement nature of the program. For example, what impact might a negative program review or OIG audit and a $750,000 previous "overaward" have on institutional participation/student access to their GSL allocation. Could the Secretary of Education exercise his "emergency powers" and terminate a school?

5. Will the demonstration provide an "opt out" opportunity for those institutions not wishing to provide loans directly or collect them? If so, will the demonstration test the Department of Education's capacity to administer an alternative loan delivery system?

USSA believes an institution's desire to avoid participation should be honored, however the college or university's decision should not deprive its students of any benefit to which he or she would otherwise be entitled, e.g. higher loan limits, flexible or extended repayment options, etc. The institutional option should be preserved while assuring each student of the same benefits irrespective of the participation or non-participation of the student's institution in the direct loan program. An alternative delivery system must be present and tested in the demonstration—either the Department of Education, Sallie Mae, or state-based alternative, etc.

6. Will the participating institutions administer both GSL's and direct loans during the demonstration?

Yes, we believe that each institutions should be required to administer both programs simultaneously, since they will do so initially if direct lending is fully implemented after the demonstration. In addition, institutional prerogatives would be preserved—in the event that the demonstration proves the anticipated savings and efficiencies contemplated were illusory—so no institution which participated in the demonstration would totally sever its relationships with GSL lenders.

7. Should staff training be provided for institutional participants in the demonstration program?

Yes, USSA strongly supports staff training, especially for smaller and medium-sized institutions. We urge the department to also consider including student assistants who work in student aid offices in this training to the extent practicable.

8. Should income contingent and flexible repayment options be included in the demonstration?

USSA strongly supports flexible repayment provisions, at the student's option, in any direct lending program.

PREPARED STATEMENT OF ELIZABETH M. HICKS, COORDINATOR OF FINANCIAL AID FOR HARVARD UNIVERSITY, CAMBRIDGE MA

I am writing concerning the income dependent education assistance program contained in Part D of the Higher Education Act of 1965 as amended by S. 1150. Before I comment on this provision of the bill, I commend you for the vision and leadership you demonstrated as chair of the Labor and Human Resources Committee and one of the principal architects of this bill. This legislation will expand student aid to middle-income families, increase Federal grants and loans, and simplify the process of applying for and receiving student aid. On behalf of the students from all sectors of postsecondary education who will benefit from this legislation, I express appreciation to you and your colleagues for making this important investment in our country's future.

I am also grateful for the work your committee did on the exploration, analysis, and ultimately the passage of a direct lending program with income-sensitive payback through a Federal agency. Enclosed please find a copy of a paper entitled "Back to the Future: Making the Case for Direct Lending," which I recently presented before the annual meeting and student loan seminar of the Coalition of Higher Education Assistance Organizations. As a result of conversations with my colleagues, I believe that my comments reflect the views of educational institutions across the Nation that are interested in pursuing the creation of a direct lending program to address the problems of access, cost, and quality in the current Guaranteed Student Loan (GSL) program.

In my paper I state that the fundamental concept of the Guaranteed Student Loan program—whereby Federal expenditures are leveraged to generate private, capital—has changed very little from its beginnings in the mid-1960's. What has changed is the nature of the students and families the GSL program serves and the environment in which the program operates. The current GSL program is an inappropriate structure in the present environment because it directs limited Federal dollars to the burgeoning administrative bureaucracies required to support the program, rather than to students in need of funds for their educational expenses. While I have few doubts that we could replace the Federal guarantee loan program with a Federal direct loan program without disrupting the flow of dollars to students, I understand that others are recommending that we proceed more cautiously.

The self-reliance loans authorized under the income dependent education assistance program are an important step in the right direction. For the most part, these loans meet the benchmarks of the ideal student loan program identified in the attached paper. However rather than creating a new loan program, I recommend that you seize this opportunity to begin substituting a Federal direct loan program for the Federal Guaranteed Student Loan program by establishing self-reliance loans as a replacement for the Supplemental Loans for Students (SLS) program. I also recommend that you expand the number of participating schools to more than a cohort of 300. This number is less than 4 percent of the schools in the current GSL program and is insufficient to provide for cooperation in systems building among institutions. At minimum, we ideally need 800 schools in order to have a critical mass participating in self-reliance loans in each region or state.

I appreciate this opportunity to comment on direct lending and to again congratulate you and your colleagues in the Senate, and in particular on the Committee of Labor and Human Resources, for the fine work you have accomplished to date on behalf of America's next generation.

BACK TO THE FUTURE: MAKING THE CASE FOR DIRECT LENDING

I. Introduction

One of the most controversial debates during the current reauthorization is whether the Federal Government should move from a guarantee student loan program to a direct loan program. Without a careful review of direct lending, there is a temptation to assume that it is either a return to a past failure or a risky experiment for the future.

Nothing could be further from the truth. Direct lending is neither the rebirth of a prior program that failed, nor is it a major innovation yet untried. Rather, direct lending is the application of successful components of several past financial aid programs to the present environment, with the goal of ensuring the perpetuity of our largest Federal student financial aid program well into the future.

The purpose of my presentation is to explain how direct lending will take us "Back to the Future." After a brief background of the Guaranteed Student Loan program, I will highlight the benchmarks of an ideal student loan program and explain why direct lending meets those standards. We will examine how direct lending works and conclude by exploring what the future holds. Throughout, my basic premise is that a guarantee loan program is outdated and a direct loan program timeless.

II. Background

The fundamental concept of the Guaranteed Student Loan program—whereby Federal expenditures are leveraged to generate private capital—has changed very little from its beginnings in the mid-1960's. What has changed is the nature of the students and families the GSL program serves and the environment in which the program operates.

—Originally directed to middle-income families experiencing cash flow problems, the GSL program now is used to meet the demonstrated financial need of Federal student aid applicants from low- and middle-income backgrounds.
—Initially serving students at a few public and private institutions, the GSL program now serves students enrolled in thousands of institutions from all sectors of postsecondary education.
—Formerly a program used to award the last dollars for student's educational costs, the GSL program now is used to distribute the first dollars for students' direct educational and living expenses.
—In the beginning a program that awarded millions of dollars annually to students, the GSL program now awards billions of dollars each year.

These changes have stretched the limits of the GSL program too far. The program was originally designed to operate on a smaller scale. A student borrowed all his loans from the family's neighborhood bank and the lender held and serviced the borrower's entire loan portfolio throughout the life of the loans.

But economies of scale have rendered this personal approach impractical, if not impossible. Lenders now have no prior banking relationship with the borrower, conduct most of their business with the borrower by mail, offer 24 hour loan processing in order to compete, contract out loan servicing, and sell loans as needed to secure capital—sometimes even before the loan is disbursed, and often without informing the borrower.

In addition to the student, the school, the lender, and the Federal Government, this private-Federal partnership now includes the guarantee agency, the servicer, the secondary market, and the collection agency. Further, since the original design of the GSL program did not take into account a growth industry of servicers, there is less oversight of these entities, which has recently resulted in improper servicing of millions of dollars worth of loans.

The GSL program carries with it the seeds of its own destruction. It is an inappropriate structure in the present environment because it directs limited Federal dollars to the burgeoning administrative bureaucracies required to support the program, rather than to students in need of funds for their educational expenses.

During the past year, many Federal legislators, educational associations, and educational institutions have concluded that simply changing the current GSL program will not address its multitude of problems. The next logical progression—to restructure the program—is necessary. With this thought in mind, several proposals have been developed to create an ideal student loan program.

III. The Ideal Student Loan Program

The ideal student loan program serves the needs of the borrowers for whom it is intended, results in the most effective expenditure of the lender's funds, and provides reasonable assurances that the funds will be repaid. The benchmarks I have identified for the ideal student loan program can be summarized as follows. The ideal student loan program:

—is responsive to the needs of the borrower
—is understandable to the borrower
—is administratively manageable and effective
—keeps administrative costs to a minimum
—ensures program accountability and integrity
—provides assurance for capital demands
—is equitably available to all potential borrowers
—has beneficial terms for borrowers
—protects the rights of the lenders
—results in timely delivery of the loan proceeds

A careful evaluation—by those in the best position to make such judgments—of these, and similar value descriptions, against the current GSL structure indicates the program is in need of change. At its November 1991 Board of Directors meeting, NASFAA did not fully endorse current Federal direct loan proposals, but recommended development and implementation of a parallel direct loan program, with no limitations on the number of schools that could participate. In a letter to the NASFAA membership, Dallas Martin, the President, shared the Board's evaluation of the current GSL program against their ideal student loan "value descriptions." The letter states:

> Generally speaking, there was nearly unanimous agreement that the existing GSL program has a number of deficiencies that need to be addressed to make the program more understandable and responsive to students, to improve administrative efficiency, and to ensure program integrity. The Board particularly favored proposals which would standardize application, deferment, and reporting documents and efforts to reduce origination fees and administrative complexity for students. Many Board members expressed genuine frustration with the time delays and difficulty they experience in providing quality service to student borrowers under the current structure.

On the other hand, direct lending fared quite well when the NASFAA Board of Directors measured it against their value descriptions. The letter continues:

> For these reasons, many members favored the direct lending proposals, believing that institutions could originate loans, disburse funds, and make needed adjustment much more effectively and without the delays and inconvenience that now occurs at many schools. Further, the idea of reducing the number of entities that students must deal with to initially secure their loans was seen as a very positive feature of the direct lending proposals. A majority of Board members also strongly favored the House direct lending approach which would eliminate student insurance and origination fees.

IV. How Direct Lending Works

Some of the most adamant critics of direct lending are those that make erroneous assumptions about the program and how it will operate. One incorrect assumption is that direct lending is the Guaranteed Student Loan program with the school as the lender—that is, something akin to the previous Federally Insured Student Loan program. A direct loan program would be more similar in concept to the Pell Grant program, or the Perkins Loan program, with some notable differences.

In order to comprehend how direct lending works, it is important to understand the similarities and differences of direct lending with the Guaranteed Student Loan program, the Perkins Loan program, and the Pell Grant program.

A COMPARISON OF DIRECT LOANS AND THE GUARANTEED STUDENT LOAN PROGRAM

A Direct Loan program and the Guaranteed Student Loan program share the following features as both:

—Are an entitlement program.
—Have no limit on the amount of capital.
—Have capital availability determined by student and parent eligibility only.
—Have eligibility for subsidized loans based on financial need.

Direct lending differs from the Guaranteed Student Loan program as under direct lending:

—The capital is secured at wholesale, rather than retail, rates.
—The program is financed through the sale of government securities, not through commercial lenders.
—Government subsidizes are targeted to students, not to the administrative bureaucracies required to support the program.
—The multiplicity of guarantee agency policies and procedures is eliminated.
—The process is transparent to the student.
—The resolution of overawards and refunds is more easily facilitated.

A COMPARISON OF DIRECT LOANS AND THE PERKINS LOAN PROGRAM

A Direct Loan program and the Perkins Loan program share the following features as under both:

—There is no need for the borrower to complete a separate loan application in addition to the Federal student financial aid application.
—The school is able to disburse and deliver the loan along with the rest of the student's financial aid package.
—Schools have direct control over the timing and distribution of loan funds.
—The school secures the student's properly endorsed signature on a standardized promissory note.

Direct lending differs from the Perkins Loan program as under direct lending:

—There is no limit to the amount of capital.
—Schools are not required to submit an institutional application to secure a level of funding.
—Schools are not the lenders and never own the loans.
—Schools are not responsible for the servicing and collection of loans, or for contracting these services.
—Schools are not required to provide long-term storage of promissory notes, but rather transmit signed promissory notes to the school's designated servicing contractor.

A COMPARISON OF DIRECT LOANS AND THE PELL GRANT PROGRAM

A Direct Loan program and the Pell Grant Program share the following features as under both:

—At the beginning of each award year a school is given an initial authorization, which is adjusted as the award year progresses based on the actual number of eligible students.
—A school draws down funds from the Department of Education's Payment Management System.

Direct lending differs from the Pell Grant program as under direct lending:

—There is no limit on the amount of capital.
—Receipt of funds is not dependent on the submission of a separate voucher for each student, such as the Pell Grant Student Aid Report.

TEN BASIC STEPS TO APPLY FOR AND RECEIVE A DIRECT LOAN

Here are the ten basic steps involved in applying for and receiving a direct loan:

Step 1—A student completes a Federal financial aid application to apply for all forms of title IV aid. There is no additional application for a direct loan.
Step 2—The student submits the application to a processor.
Step 3—The processor computes a student's eligibility according to the Federal need analysis and conducts central data base matches with entities such as Selective Service, the Immigration and Naturalization Service, the Department of Justice, and the National Student Aid data base.
Step 4—The processor forwards its result, including default analysis, to the school.

Step 5—The school reviews the need analysis, determines the student's eligibility for all forms of title IV aid, and sends the student an award notice.

Step 6—The school secures the student's signature on a standardized promissory note and ensures that the note is properly executed.

Step 7—The school draws down the funds from the Department of Education's Payment Management System and posts the funds to the student's account within time frames consistent with existing procedures.

Step 8—The school conducts entrance loan interviews with new borrowers. A school can credit a new borrower's account, but cannot advance loan proceeds to a new borrower prior to the completion of the entrance loan interview.

Step 9—The school transmits the promissory note to the Department of Education's servicing contractor.

Step 10—The school originally reports essential data elements to the Department of Education's contractor such as: Enrollment status and amount of loan. The school also updates this information with the contractor as necessary, based on change in enrollment status or amount of loan disbursed, including refunds and overpayments.

V. Exploring the Future

The future holds the possibility of either failure or success, depending on the path we choose.

If We continue on our present course with the Guaranteed Student Loan program, we will end up spending more to make loans to fewer students. To bring escalating default costs under control, Congress and the Department of Education will continue to micro-manage the program. There will be little or no possibility of performance bonuses for those entities that administer the program effectively.

I agree that we could improve the current GSL structure by standardizing policies, procedures, and forms and by making better and common use of new technologies. And I hope that you would agree that, to date, lenders, guarantee agencies, secondary markets, and servicers have failed to do this on their own initiative.

I also agree that the creation of the National Student Aid Data base would be of the same benefit to the GSL program as it will be to direct lending.

But, I also believe that the centralization that would occur under direct lending—which is the same as that under the Perkins Loan program—will lead to a faster and smoother transition to this standardization. In addition, the creation of direct lending will provide the needed incentive to make the completion of the National Student Aid Data base a top priority.

In the final analysis, the one irrefutable fact is that the current GSL program will cost more than direct lending because it obtains capital at retail, rather than wholesale, rates. If you do not believe me, ask any child old enough to understand the concept of borrowing and interest whether he would want to borrow a loan at x interest rate, or x interest rate plus 3.25 percent. Without the cost savings direct lending produces, the future of our largest Federal student loan program is not bright.

VI. Conclusion

I began this presentation on the merits of direct lending with the "Back to the Future" analogy. For those of who you are not movie buffs, or did not see "Back to the Future I, II, or III." you may be unfamiliar with the plot of this science fiction trilogy and the struggle of the protagonist which is central to all three films.

The plot is straightforward. A successful time machine is invented which provides the protagonist with an opportunity to travel at random from the present, into the past, on to the future, and back again. knowing exactly what the future holds, the protagonist struggles with whether he should change the course of destiny by effecting the outcome of critical events.

I am not trying to portray these movies as deep philosophical works of art. They were simply made to be entertaining, and they are. I am using this analogy in the hopes that if I leave you with only one message it is the following.

We do not need to travel into the future to know that direct loans will result in considerable cost savings. Responsible analysts in the Congressional Budget Office, the General Accounting Office, and the Department of Education have told us so. We do not need to travel into the future to know that schools can, and will, more effectively originate loans than commercial lenders. Our past experience with the Perkins Loan program proves that. We do not need to travel into the future to know that direct loans will better serve borrowers. Confused, and often desperate students and their families, are telling us now that they need a simple and understandable program.

Unfortunately, we are at a point in time when the current GSL program is beginning to show the signs of serious systemic problems. But fortunately, we are also at a point in time where a number of events are converging that make direct lending a possibility. Recent international events, as well as the credit reform act, provide us with an opportunity to reprioritize our Federal spending and invest funds in our Nation's youth. We have several members in both the House and Senate who have shown the vision and leadership to promote creative direct lending proposals. We have universities and colleges that are willing, on behalf of their students, to commit time and energy to help make direct lending a success.

As the protagonist in "Back to the Future," we have the ability to change the course of destiny—in our case, by replacing the Federal guarantee loan program with a Federal direct lending program. If we do not intervene, but rather continue on our present course, we will endanger our largest Federal student financial aid program. But more importantly, we will risk access to higher education for the very individuals who must be in the forefront of our future efforts to remain among the world's leading nations. We cannot let this moment of opportunity escape, for—unlike the protagonist in "Back to the Future"—we are not in a time machine and will never pass this way again. Thank you.

PREPARED STATEMENT OF DR. NORMA E. WAGONER, DEAN OF STUDENTS, UNIVERSITY OF CHICAGO PRITZKER SCHOOL OF MEDICINE ON BEHALF OF THE AMERICAN ASSOCIATION OF COLLEGES OF NURSING, AMERICAN ASSOCIATION OF COLLEGES OF PHARMACY, AMERICAN ASSOCIATION OF COLLEGES OF PODIATRIC MEDICINE, AMERICAN ASSOCIATION OF DENTAL SCHOOLS, ASSOCIATION OF ACADEMIC HEALTH CENTERS, ASSOCIATION OF SCHOOLS OF ALLIED HEALTH PROFESSIONS, ASSOCIATION OF AMERICAN MEDICAL COLLEGES, ASSOCIATION OF AMERICAN VETERINARY MEDICAL COLLEGES, ASSOCIATION OF SCHOOLS OF PUBLIC HEALTH, AND ASSOCIATION OF UNIVERSITY PROGRAMS IN HEALTH ADMINISTRATION

Good morning. My name is Norma Wagoner. I am the Dean of Students at the University of Chicago Pritzker School of Medicine. In my capacity as Dean of Students and an associate dean, I have been directly involved in the management and awarding of financial aid for the past sixteen years. I am here today to testify on behalf of several professional school associations representing schools of allopathic medicine, dentistry, nursing, pharmacy, podiatry, veterinary medicine and public health, and programs in health administration and allied health, and academic health centers, as well as over 200,000 students enrolled at institutions providing these programs.

This morning I would like to focus my remarks on why income sensitive repayment would be beneficial to health professions students.

Indebtedness and access to financial aid are particular concerns in health professions education. Federal grant support is available only to a small portion of our students. Hence, the vast majority of our health professions students must borrow to finance their educations and graduate with considerable debt burdens. The programs authorized under Tide IV of the Higher Education Act are critical sources of financial aid for our students. In fact, among the 1990 medical and dental school graduates, over 75 percent borrowed a Stafford loan, and nearly one third utilized the Supplemental Loan for Students (SLS) and the Perkins loan programs. Clearly, without Stafford Student Loans, Supplemental Loans for Students, and campus-based Perkins Loans, health professions students would find it difficult, if not impossible, to finance their education.

It is important to note, however, that title IV loan sources do not meet fully the needs of many health professions students. As these students reach the maximum borrowing levels in title IV subsidized programs, they are forced to rely on more expensive loans, such as the Health Education Assistance Loan (HEAL), with terms and conditions much less favorable than the title IV loans. HEAL borrowers currently pay an 8-percent insurance premium upon origination and are charged a floating interest rate tied to the 91-day Treasury bill. Despite the costly terms and the fact that the HEAL loan was designed as a "loan of last resort," last year HEAL was the second largest financial source behind the Stafford Student ban program for health professions students.

Although it is reasonable to expect students to borrow in order to finance graduate or professional education, the annual escalation in the level of educational debt is causing alarm in our community. Medical and dental school graduate indebtedness has increased over 75 percent in constant dollars in the last decade. Mean debt among 1990 medical and dental students was \$46,224 and \$45,550, respectively. Even more troubling than these averages are the numbers, especially of disadvantaged and minority students, graduating with debts exceeding \$50,000. In addition,

$100,000 of educational debt is not uncommon for health professions graduates. While some students in health professions disciplines such as nursing and public health have shorter periods of in-school training and may not incur these very high debt levels, the relatively lower starting salary of these disciplines intensifies the problem of repayment. Many health professionals in the higher-paid disciplines also experience difficulty in repaying their loans during the first few years after school, difficulties which are exacerbated when indebted graduates opt for lower paying careers in primary care or underserved rural and inner city settings. For example, the 1990 starting salary for a registered nurse averaged $24,768, approximately $50,000 for a general pediatrician, and approximately $40,000 for a general dentist. Some health professions graduates are interested in, but financially deterred from, such career choices. Similarly, the debt-to-income-ratio of a heavily indebted graduate can make it impossible, despite the individual's willingness, to make the required loan payments during the first few years following graduation.

It is necessary to note that many health professions students must continue in a training program, known as a residency or internship, following graduation in order to become licensed or certified. Residency training for medical school graduates lasts between three and seven years depending on the specialty, during which time the average stipend received in 1990 was approximately $27,000. Other disciplines do not require post-graduate clinical training, but many of their graduates choose to participate in internship or residency training programs to prepare them for specialty practice, such as in geriatrics. In a number of cases, these residents are required to pay tuition to participate in that supervised clinical experience. In dentistry, for example, well over half of those graduates who participate in residency programs pay tuition and receive little if any stipend. Loan repayment is particularly problematic for residents and interns.

In order to meet successfully the challenges faced by health professions students with heavy debt loads, we need to be able to offer more grants, higher loan limits on low interest loan programs, and offer more flexible repayment schedules. These steps would decrease the number of students with enormous debt, create a better balance between the grant and loan aid available, reduce overall debt burdens, curtail the instance of default, ease repayment, and facilitate the ability of health professionals to afford lower income positions in underserved areas as well as careers in primary care, teaching or research. However, federal budget constraints limit Congress' ability to offer more grants and subsidized loans, and unfortunately, the Committee's Reauthorization bill does not yet include these measures for health professions students.

We see three inherent advantages in the concept of a income-sensitive loan repayment program. First, income dependent repayment schedules factor in a graduate's earnings and aggregate level of borrowing, thereby enabling the individual to satisfy the educational debt in a manner formulated on his or her ability to pay. Second, income sensitive loans promote simplicity in the financial aid process in a variety of ways, including allowing all borrowing to take place through one title IV program, reducing paper work burdens, eliminating the necessity of deferments or forbearance, and precluding technical defaults. Finally, through income sensitive repayment plans, prospective students can matriculate and borrow at the level necessary to finance an education leading to a public service career, without concern that their salary upon graduation will not support repayment at that level of debt.

In addition to easing repayment, any income-dependent loan proposal should provide borrowing options for students that are superior to the current system. A major component of this is realistic loan limits that would be sufficient to eliminate the need for health professions students to borrow from HEAL or other high cost programs. In setting higher loan limits and longer repayment periods, we recognize that some health professions students may pay slightly more over the life of a loan than would be the case under existing standards. This point is neutralized by the fact that borrowers would be offered an option that is responsive to the timing of their ability to repay the debt and that they could borrow with confidence that they could service the debt over time. Apprehensions related to a borrower's ability to meet educational debt obligations exists in the current system. Income sensitive repayment would remove this element of fear and represent a positive step for students, institutions, and the government.

We believe the income dependent loan proposals offer new and innovative structures for student financial aid. We would be pleased to discuss this further with committee staff and help develop details that are related to this program. On behalf of the associations I am here to represent, thank the Committee for allowing us to make these comments. I will be happy to respond to questions or to clarify or expand on my remarks.

PREPARED STATEMENT OF SENATOR DANIEL R. AKAKA, A U.S. SENATOR FROM THE STATE OF HAWAII

Mr. Chairman, I would like to express my strong support for the concept of an income contingent student loan program. I join my colleagues here today in proposing an alternative approach for financing higher education for all, especially students of middle-class families.

It is the American dream, part of the fabric of our country, that an individual can obtain an education regardless of their race, color, creed and, most importantly, their financial ability. During recent times, however, our commitment to providing equality in education has wavered. American families are finding it increasingly difficult to support their children's need to obtain a higher education.

When I attended the University of Hawaii, the average length of time a student took to graduate with a baccalaureate degree was four years. Today, the average student takes five, even six years, to graduate. Many wonder why. Some may believe that our students are unprepared or the programs are more difficult. For the majority of students, the reason it takes longer to obtain an undergraduate degree is the cost of higher education.

Today's campus population consists of a higher percentage of part-time students, students who must work in order to pay for their education. It is more common now to find students taking off a year from their studies to work in order to save enough money to return to campus. Over the past decade, the Administration has turned away from our historic commitment to provide educational opportunities to all, regardless of ability to pay.

Mr. Chairman, today, we have an opportunity to reverse this dangerous trend. We have an opportunity to pursue a progressive idea for the student loan program. It is not a new idea, but is an idea which I resurrected in the Senate last June, a concept which is based on a student's ability to repay.

Given the tremendous cost of higher education, new graduates are leaving schools with an immense financial burden. The income contingent loan program will help to alleviate this burden by deferring the financial load. Students would be required to pay back their student loans based on their income after graduation.

For example, a student who leaves school with a debt of $50,000 and obtains a job paying $15,000 a year will be required to pay back his loan based on the percentage of his income. The current program requires a student to pay back a set principal and interest amount regardless of their current income.

I have no doubt that this program will be a success once established. However, I do believe that we should proceed with caution when implementing this program. As I proposed in S. 1414, I believe it would be prudent to begin a demonstration project so that we will have a manageable system which we can fine-tune before slowly integrating all schools.

Income dependent educational assistance will not only provide equal financial opportunity to all individuals seeking a higher education—it will also help to alleviate the high default student loan rate in our current loan programs.

Mr. Chairman, I urge my colleagues to join this effort to establish an income contingent student loan program, and I appreciate the opportunity to express my support for this important program.

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DISCUSSION DRAFT II
February 24, 1992

102D CONGRESS
2D SESSION

S. ____

IN THE SENATE OF THE UNITED STATES

Mr. KENNEDY (for himself, Mr. BRADLEY, Mr. SIMON, and Mr. DURENBERGER) introduced the following bill; which was read twice and referred to the Committee on ____________

A BILL

To amend part D of title IV of the Higher Education Act of 1965 to provide for income dependent education assistance.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. INCOME DEPENDENT EDUCATION ASSISTANCE.

(a) IN GENERAL.—Part D of title IV of the Higher Education Act (20 U.S.C. 1087 et seq.) is amended to read as follows:

"PART D—INCOME DEPENDENT EDUCATION ASSISTANCE

"SEC. 451. PURPOSE.

"It is the purpose of this part to establish a direct loan program for eligible students enrolled in institutions of higher education with income contingent repayment of such loans occurring through the Secretary of the Treasury.

"SEC. 452. PROGRAM AUTHORIZED.

"(a) IN GENERAL.—The Secretary is authorized to carry out a program that—

"(1) makes loans to eligible students at institutions of higher education to enable such students to study at such institutions; and

"(2) establishes an account for each borrower of such a loan, and collects repayments on such loans, in accordance with section 59B of the Internal Revenue Code of 1986.

"(b) DESIGNATION.—

"(1) PROGRAM.—The program assisted under this part shall be known as the 'income dependent education assistance program'.

"(2) LOANS.—Loans made under this part shall be known as 'self-reliance loans'.

"(c) PAYMENTS.—

"(1) PAYMENT AUTHORITY.—The Secretary shall make payments to a participating institution on the basis of the estimated borrowing needs (provided to the Secretary by such institution) of the students at such institution pursuant to guidelines developed by the Secretary.

"(2) INITIAL PAYMENTS.—The Secretary shall make initial payments under this part in a similar manner to the procedure for distribution of Pell Grants under paragraphs (1) and (2) of section 411(a).

"(d) RELATION TO OTHER FEDERAL PROGRAMS.—A participating institution shall continue to be eligible to participate in all other programs assisted under this title.

"SEC. 453. ELIGIBILITY.

"(a) STUDENT ELIGIBILITY.—

"(1) IN GENERAL.—All eligible students enrolled at a participating institution are eligible to receive self-reliance loans without regard to financial need.

"(2) CONTRACTUAL RIGHT.—An eligible student at a participating institution shall be deemed to have a contractual right against the United States to receive a self-reliance loan.

"(b) NEEDS TEST FOR STUDENTS.—Notwithstanding any other provision of law, an eligible student shall not receive a self-reliance loan in any fiscal year unless such student's eligibility for assistance under section 428 and subpart 1 of part A has been assessed.

"(c) SELECTION OF INSTITUTIONS FOR PARTICIPATION.—

"(1) IN GENERAL.—From among institutions of higher education that have submitted applications under this part and are eligible to participate in part B loan programs, the Secretary shall select institutions of higher education for participation in the income dependent education assistance program.

"(2) SELECTION OF DIVERSE SCHOOLS.—The Secretary shall select institutions of higher education for participation in the income dependent education assistance program in a manner so as to represent a cross-section of institutions of higher education by educational sector, length of academic program, default experience, annual loan volume, highest degree offered, enrollment size, and geographic location.

"(3) INITIAL SELECTION OF INSTITUTIONS.—The Secretary shall select not more than 300 institutions of higher education for participation in the income dependent education assistance program not later than May 1, 1993, except that the Secretary shall select institutions such that the projected volume of new student borrowing under this part does not exceed $450,000,000 in fiscal year 1994, $550,000,000 in fiscal year 1995, $650,000,000 in fiscal year 1996 and $900,000,000 in fiscal year 1997.

"(4) EXPANSION OF THE PROGRAM.—(A) Beginning on August 1, 1997, the Secretary shall permit all institutions of higher education that, in the opinion of the Secretary, have the administrative and fiscal capacity to administer a self-reliance loan program, if—

"(i) the Congress does not act before such date to terminate or modify such program; and

"(ii) the Congress takes the affirmative step to approve the expansion of the income dependent education assistance program by providing sufficient resources to offset the cost of the income dependent education assistance program.

"(B) The Secretary shall publish criteria to govern institutional eligibility for the income dependent education assistance program not later than September 1, 1995.

"SEC. 454. APPLICATION AND AGREEMENT.

"(a) APPLICATION.—Each institution of higher education desiring to participate in the income dependent education assistance program shall submit an application to the Secretary at such time, in such manner and accompanied by such information as the Secretary may reasonably require.

"(b) AGREEMENT REQUIRED.—Each institution of higher education chosen by the Secretary to participate in the income dependent education assistance program shall enter into an agreement with the Secretary for the receipt of funds under this part. Such agreement shall provide for the establishment of a self-reliance loan program at such institution under which such institution agrees to—

"(1) originate self-reliance loans to students, follow procedures specified by the Secretary in disbursing such loans, accept liability stemming from mismanagement of such loans, submit annual audit information, and participate in evaluations conducted by the Secretary or organizations chosen by the Secretary;

"(2) provide the Secretary at least once each month, with a list of self-reliance loan recipients and promptly notify the Secretary of changes in the enrollment status of any such loan recipient;

"(3) comply with the provisions of part B relating to loan origination, disclosure, and other matters which the Secretary determines are not inconsistent with the provisions of this part;

"(4) transfer the promissory note and other evidence of such loan as specified by the Secretary to the Secretary or the Secretary's agent within 30 days after the origination of such loan;

"(5) comply with the reporting requirements established by the Secretary;

"(6) ensure that the note or the evidence of indebtedness on the such loans shall be the property of the Secretary and that the institution will act as the agent of the Secretary for the purpose of making such loans;

"(7) counsel borrowers with regard to repayment options for self-reliance loans at the time that the borrower leaves the institution of higher education; and

"(8) contain such additional information, terms and conditions as the Secretary may prescribe to protect the fiscal interests of the United States and to ensure effective administration of the self-reliance loan program.

"SEC. 455. TERMS OF SELF-RELIANCE LOANS.

"(a) BORROWING LIMITS.—

"(1) ANNUAL LIMIT.—A student may receive a self-reliance loan in each fiscal year which does not exceed—

"(A) $5,000 in the case of an undergraduate student; and

"(B) $15,000 in the case of a graduate student.

"(2) MAXIMUM BORROWING LIMIT.—(A) The maximum amount of self-reliance loans—

"(i) an undergraduate student may borrow is $25,000; and

"(ii) a graduate student may borrow is $30,000.

"(B) The maximum amount of self-reliance loans a student may borrow shall not exceed $30,000.

"(C) The maximum amount of loans a student may borrow under this part and parts B and E shall not exceed the applicable limitations on aggregate indebtedness contained in section 428(b)(1)(B), except that, for a student determined to be independent for purposes of section 428A, the maximum amount of loans such student may borrow under this part and parts B and E shall be increased by the amount borrowed under this part not to exceed $10,000.

"(3) COST OF ATTENDANCE.—(A) No student shall receive a self-reliance loan in any fiscal year in an amount which exceeds such student's cost of attendance for such year.

"(B) The amount of financial assistance a student receives under this part in any fiscal year, when combined with student financial assistance received under other parts of this title for such fiscal year, shall not exceed such student's cost of attendance for such fiscal year.

"(b) INTEREST RATE.—

"(1) IN GENERAL.—The interest rate on self-reliance loans shall be established at the time that the loan is made and shall be equal to the interest rate on 52-week Treasury bills plus an additional 2 percentage points.

"(2) TIMING AND FREQUENCY.—The Secretary shall establish the interest rate for self-reliance loans at the same time and with the same frequency as the Secretary establishes interest rates for the Supplement Loans for Students program described in section 428A.

"SEC. 456. REPAYMENT PROVISIONS.

"(a) IN GENERAL.—A self-reliance loan shall be repayed through the income tax collection system in accordance with section 59B of the Internal Revenue Code of 1986.

"(b) REPAYMENT TERMS.—

"(1) IN GENERAL.—A borrower of a self-reliance loan or loans shall repay such loan or loans by devoting to repayment 7 percent of such borrower's adjusted gross income, except that the Secretary shall allow a borrower the option of devoting to repayment—

"(A) 3, 5, or 7 percent of such borrower's adjusted gross income in the case of a borrower who enters repayment with low indebtedness under this part, as determined by the Secretary; and

"(B) 5 or 7 percent of such borrower's adjusted gross income in the case of a borrower who enters repayment with moderate indebtedness under this part, as determined by the Secretary.

"(2) SECRETARY'S DETERMINATION OF INDEBTEDNESS LEVELS.—The Secretary shall make the determination of low indebtedness and moderate indebtedness described in subparagraphs (A) and

(B) of paragraph (1) in a manner such that the average borrower described in each such subparagraph is projected to repay self-reliance loans over a similar number of years as the average borrower with high indebtedness described in the matter preceding subparagraph (A) of paragraph (1).

"(3) REPAYMENT STATUS.—A borrower is in repayment status for any taxable year unless—

"(A) such borrower was, during at least 7 months of such year, a student enrolled in an institution of higher education on at least a half-time basis; or

"(B) such taxable year was the first year in which the borrower was such a student and the borrower was such a student during the last 3 months of such taxable year.

"(4) LENGTH OF REPAYMENT.—Repayment of a self-reliance loan shall continue until such loan has been repaid or for 25 years after the borrower ceases to be enrolled in an institution of higher education on at least a half-time basis, whichever occurs first.

"(5) SPECIAL RULE.—No repayment of a self-reliance loan shall be due in any year in which the borrower is not required to file a tax return under the Internal Revenue Code of 1986.

"(6) DETERMINATION OF ADJUSTED GROSS INCOME.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'adjusted gross income' has the meaning given to such term by section 62 of the Internal Revenue Code of 1986.

"(B) MARRIED INDIVIDUALS.—A borrower who marries an individual who has not received a self-reliance loan shall make repayments on the basis of the greater of—

"(i) one-half of the adjusted gross income shown on such borrower's joint income tax return; or

"(ii) the individual borrower's adjusted gross income.

"(c) DEFERRAL OF INTEREST.—A borrower, at the borrower's discretion, may defer payment of interest on a self-reliance loan while the borrower attends an institution of higher education on at least a half-time basis.

"(d) PREPAYMENTS.—A borrower may prepay all or part of a self-reliance loan to the Secretary without a penalty.

"(e) CANCELLATION FOR DEATH AND DISABILITY.—The Secretary shall discharge the liability to repay a self-reliance loan in the event of death or total permanent disability of a borrower.

"(f) RULES RELATING TO BANKRUPTCY.—

"(1) IN GENERAL.—A self-reliance loan shall not be dischargeable in a case under title 11 of the United States Code.

"(2) CERTAIN AMOUNTS MAY BE POSTPONED.—If any individual receives a discharge in a case under title 11 of the United States Code, then the Secretary may postpone any amount of the portion of the liability of such individual on any self-reliance loan which is attributable to amounts required to be paid on such loan for periods preceding the date of such discharge.

"SEC. 457. RESPONSIBILITIES OF THE SECRETARY.

"(a) TERMS AND CONDITIONS.—The Secretary shall promulgate the terms and conditions of a self-reliance loan not otherwise specified in this part.

"(b) ENFORCEMENT.—The Secretary shall have the same authority to limit, suspend or terminate an institution of higher education's ability to participate in the income dependent education assistance program as the Secretary has to terminate an institution of higher education's participation under a part B loan program. The Secretary may specify by regulation additional criteria the

Secretary shall use to monitor the performance of participating institutions.

"(c) CENTRAL DATA SYSTEM.—The Secretary shall develop and administer a central data system for use in administering self-reliance loans. Such data system shall—

"(1) permit borrowers to secure information on their accounts;

"(2) on at least an annual basis, provide each self-reliance borrower with a statement of account balance and information on prepayment options; and

"(3) permit the processing of borrower payments received, including the generation of confirmations to borrowers.

"(d) STATEMENTS.—

"(1) IN GENERAL.—The Secretary shall, not later than January 1 of each year, certify to the Secretary of the Treasury for each borrower in repayment status on such date an amount equal to the sum of the total principal amount of loans made to such borrower plus any accrued interest minus the sum of any amounts collected from such borrower. A copy of such certification with respect to a borrower shall be sent by the Commissioner of the Internal Revenue Service to such borrower.

"(2) SPECIAL RULE.—Any borrower who receives a notice of certification under paragraph (1) and who believes such notice contains an error of statement or omission, or asserts a debt for which the borrower is not obligated or to which the borrower desires to raise a defense or excuse, shall file an objection thereto with the Secretary within 60 days after receipt of such notice. The Secretary shall, within 30 days of receipt of such an objection, affirm, adjust, or withdraw such certification and send notice thereof to the borrower and to the Secretary of the Treasury. Such decision shall be reviewable by an appropriate district court of the United States as a final agency decision.

"(e) STANDARD FORMS AND DATA FORMATS.—The Secretary shall develop standard forms and data formats for use by institutions of higher education and borrowers regarding self-reliance loans.

"(f) IMPLEMENTATION REPORT.—The Secretary, in consultation with the Secretary of the Treasury, not later than 1 year after the date of enactment of this part, shall provide a report to the Congress describing the implementation of the income dependent education assistance program, especially the steps taken to implement the loan repayment provisions described in section 456, and identifying problems that require legislative action.

"(g) ANNUAL REPORT.—The Secretary, beginning January 1, 1995, shall provide an annual report to the Congress evaluating the implementation and administration of the income dependent education assistance program and identifying problems that require legislative action.

"(h) EVALUATION.—Not later than January 1, 1997, the Secretary, in consultation with the Secretary of the Treasury, shall make a report to the Committee on Education and Labor of the House of Representatives and the Committee on Labor and Human Resources of the Senate evaluating the income dependent education assistance program. Such report shall—

"(1) analyze the administrative burden and cost imposed on the Department of Education and any other agency of the Federal Government by the income dependent education assistance program;

"(2) analyze the administrative capacity of the Department of Education and any other agency of the Federal Government to operate a self-reliance loan program at all institutions of higher education;

"(3) analyze the administrative and financial obstacles that may preclude all institutions of higher education from operating a self-reliance loan program and make recommendations for corrective action;

"(4) analyze the complexity of the income dependent education assistance program for institutions of higher education and students in comparison with the complexity of part B loan programs for institutions and students participating in loan programs under part B;

"(5) determine whether borrowers are better informed about their loan obligation under this part compared to other part B loan programs;

"(6) analyze the impact of the income dependent education assistance program on repayments, delinquencies and defaults;

"(7) make any recommendations for legislative action that may be needed to facilitate the implementation of the income dependent education assistance program to all eligible institutions of higher education;

"(8) publish the cost of tuition and the cost of attendance at each participating institution and analyze changes in such costs compared to such changes occurring in institutions of higher education that do not participate in the income-dependent education assistance program;

"(9) analyze the ability of the Department of Education to serve students in accordance with the income dependent education assistance program; and

"(10) analyze the effect of borrowing under the income dependent education assistance program on part B loan programs, including the effect on—

"(A) the socioeconomic status of students participating in part B loan programs;

"(B) the lenders, guarantee agencies and secondary markets participating in part B loan programs; and

"(C) the rate of defaults in part B loan programs.

"(i) OVERSIGHT RESPONSIBILITY AND DELEGATION.—The Secretary shall be responsible for all oversight of participating institutions.

"SEC. 458. DEFINITIONS.

"For purposes of this title—

"(1) the term 'cost of attendance' has the same meaning given to such term by section 472;

"(2) the term 'eligible student' means a student who is a United States citizen and has attained the age of 17 but not the age of 51;

"(3) the term 'institution of higher education' means an institution of higher education (as such term is defined in section 481(a)) which as demonstrated the administrative and fiscal capacity to carry out the provisions of this part; and

"(4) the term 'participating institution' means an institution of higher education having an agreement with the Secretary pursuant to section 454(b).".

SEC. 2. COLLECTION OF LOANS.

(a) IN GENERAL.—Subchapter A of chapter 1 of the Internal Revenue Code of 1986 (relating to determination of tax liability) is amended by adding at the end thereof the following new part:

"PART VIII—EDUCATIONAL LOAN REPAYMENT TAX

"SEC. 59B. EDUCATIONAL LOAN REPAYMENT TAX.

"(a) IN GENERAL.—The Secretary of the Treasury shall enter into an agreement with the Secretary of Education to provide for the collection of repayments of self-reliance loans due pursuant to part D of title IV of the Higher Education Act of 1965.

(b) DETERMINATION OF TAX.—In the case of an individual who receives a certification from the Secretary of

Education under section 457(d) of the Higher Education Act of 1965, there is hereby imposed (in addition to any other tax imposed by this subtitle) a tax equal to the repayment percentage (as certified by the Secretary of Education) of the taxpayer's adjusted gross income for the taxable year.".

(b) CLERICAL AMENDMENT.—The table of parts for subchapter A of chapter 1 of such Code is amended by adding at the end thereof the following new item:

"Part VIII. Educational loan repayment tax.".

Senator SIMON. We appreciate your being here, and the hearing stands adjourned.

[Whereupon, at 1:15 p.m., the committee was adjourned.]

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