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National Student Loan Program

Carnegie Commission on Higher Education

NATIONAL STUDENT LOAN PROGRAM

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It is the conviction of the Commission that the student from a low-income family should receive enough money through grants and work-study payments to enable him to attend a low-cost college near home. If, however, such a student wishes to select a higher-cost institution, or an institution at a greater distance from home, he should be able to obtain a long-term loan to cover these additional costs. The grant and work-study programs thus provide the low-income student with initial access to higher education, while the loan program provides some measure of mobility.

It is assumed that the student from a middle-income or higher-income family will have initial access to higher education through family contributions. He also, however, may wish to increase his range of choice by borrowing to supplement the family contributions or to increase his independence by borrowing to decrease his reliance on family contributions.

To provide this supplementary source of financial aid for needy students and to provide a substantial source of financial aid for middle-and higher-income students, the Commission recommends that the federal government charter a National Student Loan Bank, a nonprofit private corporation to be financed by the sale of governmentally guaranteed securities. The Bank would make loans available to postsecondary students in amounts not to exceed $2,500 per year up to a total of $6,000 for undergraduate studies and $10,000 for graduate studies. No student would be eligible to obtain more in loans, all types of grants, and work-study payments in any year than his costs of education, including subsistence costs, as officially recognized by the institution in which the student is enrolled. The Bank would be self-sustaining, except for administrative costs and the cost of any cancellations of interest because of low income and of principal for any reason other than death, which would be met out of federal budget appropriations.

LEVEL OF FUNDING

The level of funding provided for the Student Loan Bank should be high enough to provide the funds needed by students, but the loan component of student aid should not be permitted to increase to the extent that it is viewed

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as the dominant source of funding for student financial aid, nor should it be allowed to grow to the point where it permits substantial upward pressures on tuition levels.

The Commission proposes that approximately $3 billion in new loans be authorized for the first two years of the Bank's existence. This level of funding would leave well over 90 percent of the total costs of postsecondary education to be met from other public and private sources. After the first two years, new annual obligation levels would be set each year by agreement between the Directors of the Bank and the Secretary of the Treasury.

REPAYMENT PROVISIONS

Borrowers would be required to repay loans by paying at least three-fourths of 1% of income each year for each $1,000 borrowed until the total loan and accrued interest was repaid. Each payment would be applied first to accrued interest and then to principal. This level of repayment would permit the average income earner to repay his loan in approximately 20 years.

For borrowers filing a joint tax return, the appropriate rate of repayment for the combined debt of the husband and wife would be applied to the combined income of the husband and wife.

The initial installment would not be due and payable until two years after earning an undergraduate degree (or discontinuing studies at the undergraduate level) or one year after earning a graduate degree (or discontinuing studies at the graduate level).

Annual repayments would be deferred at the option of the borrower for any or all of the following periods:

1. During a maximum of three years service in the armed forces, Peace Corps, VISTA, and other programs designated by the President as similar national service programs, or
2. During any period in which the income of the borrower (or the combined income of husband and wife in the case of a borrower filing a joint tax return) falls below a certain minimum subsistence level which shall be periodically determined by the Bank.

COLLECTION

The Bank would be authorized to enter into an agreement with the Department of the Treasury under which the Internal Revenue Service would undertake all collections. Costs incurred by IRS in providing this service should be met by the Bank.

INTEREST

The interest rate charged the student would be set at a level which is adequate to permit the Bank to obtain the funds and to cover cost of cancellation upon the death of the borrower. Because of the governmental guarantee of the Bank's securities, this rate would be somewhat below the commercial rate.

Interest which accrued prior to the initial repayment installment would be added to the principal.

INTEREST CANCELLATION

Up to 50 percent of the amount of interest added to the principal before the payment of the first installment, and up to 50% of the amount of interest accrued in any given year after repayment begins, may be cancelled in accordance with a sliding scale to be determined by the Directors of the Bank, thus permitting interest reduction for borrowers with low income.

CANCELLATION OF PRINCIPAL

There shall be no cancellation or forgiveness for entering particular professions. Any remaining indebtedness shall be cancelled upon the death of the borrower or at the end of 30 years from the date of first payment. Disability shall not be cause for cancellation of any portion of principal, but to the extent it results in low income, it may be cause for partial interest cancellation or for deferral of payments. If disability continues to death or the expiration of the 30-year period, the deferred payments, just as would the remaining balance, will be cancelled.

The Commission urges that consideration be given to amending the Bankruptcy Act to exempt amounts owed to the Bank from those debts which may be discharged in a bankruptcy proceeding.

BURDEN OF REPAYMENT

It is assumed that few students would borrow up to the maximum limits allowed. Those students who do borrow up to the limit of $16,000 undoubtedly would have completed a graduate or professional degree and would have higher earnings from which to repay their loan.

Assuming an undergraduate student borrows the maximum of $6,000 ($1,500 each year beginning in 1970) and that the interest rate is set at 7%, his principal plus interest debt at time of his first payment would be $6,960. Assuming a 4% annual increase in salary levels, by 1975 when the student begins making payments on the loan, it is estimated that a typical college graduate would be earning about $10,000 a year, and his first annual payment would be $450 (4½% representing three-fourths of 1% for each $1,000 borrowed). As his income rises, the absolute amount of repayment would rise, but the proportionate burden on his income would remain the same. If salaries continue to increase at their present rate, in 10 years his annual salary would be $14,802, and his payment would be $666. With a continued rise in salary and payment level, his loan would be repaid in 22 years. A shorter period would be required if his salary rose more rapidly than the general level of salaries.

For the student from a low-income family, the burden would be somewhat less because a portion of interest (up to one-half depending upon income level) accrued before the first payment would be cancelled. The burden is similarly reduced for the borrower in any year in which he has a low income. This later reduction is without regard to his income or the income level of his family while he was a student.

ALTERNATIVE

The Commission believes that establishment of a National Student Loan Bank is the best vehicle for providing desirable levels of funding and appropriate terms for student loans.

If, however, it does not seem feasible at this time to establish a National Student Loan Bank as recommended by the Commission, it does seem desirable as a current measure designed to increase the availabiltiy of funds for students to establish a secondary market such as the proposed National Student Loan Association. Because of the difficulty of changing the authorizations for such organizations once chartered, the Commission recommends that the original charter for any such secondary market be broad enough to empower it to grant loans if further experience indicates the desirability of this course of action.

Any student loan program should be viewed as experimental and subject to change with greater experience.

The Commission further recommends that, if any existing loan programs are extended and supported by the addition of a secondary market, all the above proposed modifications in terms and conditions of the student loan program be adopted at the time of extension to the extent it is possible to do so without establishment of a Bank.

There are, however, circumstances in which a general student subsidy would be desirable. In such circumstances, a subsidy could easily be built into a comprehensive loan program by setting interest to the borrower substantially below the rate necessary to allow the Bank to be self-sustaining or by requiring that only a certain portion of the principal be repaid.

Whether the loan program established is that proposed by the Commission or some variation of that proposal, it should be a single comprehensive program covering all students with the exception of medical students — for whom the Commission will make separate recommendations. The essential components of a comprehensive loan program are:

- Funds for loans should be readily and assuredly available at a steadily adequate level.

- The loaning agency should not require any collateral from the student borrower, nor should borrowers be required to maintain deposits with the loaning agency.

- The loan program should include features which would result in the government sharing some of the risk for low-income years during the repayment period.

- Both the conditions for eligibility and the amount of loans permitted should be such that students are afforded a substantially expanded range of educational options.