# ENSURING THE AVAILABILITY OF FEDERAL STUDENT LOANS

## HEARING

BEFORE THE

## COMMITTEE ON EDUCATION AND LABOR

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

HEARING HELD IN WASHINGTON, DC, MARCH 14, 2008

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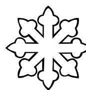

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# ENSURING THE AVAILABILITY OF FEDERAL STUDENT LOANS

**Friday, March 14, 2008**
**U.S. House of Representatives**
**Committee on Education and Labor**
**Washington, DC**

The committee met, pursuant to call, at 9:00 a.m., in room 2175, Rayburn House Office Building, Hon. George Miller [chairman of the committee] presiding.

Present: Representatives Miller, Kildee, Payne, Andrews, Scott, McCarthy, Tierney, Kucinich, Holt, Grijalva, Timothy Bishop of New York, Sanchez, Sarbanes, Loebsack, Altmire, Yarmuth, Hare, Clarke, Courtney, Shea-Porter, McKeon, Petri, Souder, Ehlers, Platts, Keller, Wilson, Kline, Price, Kuhl, Bishop of Utah, Davis of Tennessee, and Walberg.

Staff Present: Tylease Alli, Hearing Clerk; Jeff Appel, Senior Education Policy Advisor/Investigator; Sarah Dyson, Administrative Assistant, Oversight; Carlos Fenwick, Policy Advisor, Subcommittee on Health, Employment, Labor and Pensions; Patrick Findlay, Investigative Counsel; Denise Forte, Director of Education Policy; Gabriella Gomez, Senior Education Policy Advisor; Lloyd Horwich, Policy Advisor, Subcommittee on Early Childhood, Elementary and Secondary Education; Lamont Ivey, Staff Assistant, Education; Thomas Kiley, Communications Director; Ann-Frances Lambert, Administrative Assistant to Director of Education Policy; Danielle Lee, Press/Outreach Assistant; Stephanie Moore, General Counsel; Alex Nock, Deputy Staff Director; Joe Novotny, Chief Clerk; Rachel Racusen, Deputy Communications Director; Julie Radocchia, Education Policy Advisor; Dray Thorne, Senior Systems Administrator; Michele Varnhagen, Labor Policy Director; Margaret Young, Staff Assistant, Education; Mark Zuckerman, Staff Director; Julia Martin, Intern; Stephanie Arras, Minority Legislative Assistant; James Bergeron, Minority Deputy Director of Education and Human Services Policy; Robert Borden, Minority General Counsel; Amy Raaf Jones, Minority Professional Staff Member; Alexa Marrero, Minority Communications Director; Susan Ross, Minority Director of Education and Human Services Policy; Linda Stevens, Minority Chief Clerk/Assistant to the General Counsel; Sally Stroup, Minority Staff Director.

Chairman MILLER. The Committee on Education and Labor will come to order for the purposes of conducting this hearing on ensuring the availability of student loans. The purpose of this hearing

is to provide information to the committee and to students, their families and their schools about our ability to assure them that student loans will continue to be made available to them and the development of contingency plans in the unlikely event that some lenders are unable to continue lending in this market.

In some cases, we have been forewarned that some lenders will not lend or will reduce their lending, and in other cases, we have been told by some lenders that they will expand their lending, and we are trying to balance that information. This is really about us making the proper preparations so that in the upcoming lending season for students in their school year and for their families, we will be able to make sure that there is a seamless system in place so that we can use already existing legal authority and programs that are on the books, whether that is the Lender of Last Resort provisions in the law or whether that is the Direct Lending program.

Senator Kennedy and I sent the Secretary a letter outlining why we thought it was necessary to have plans in place so that we can deal with these contingencies. Under the existing laws, some 35 guarantee agencies around the country are obligated to serve as lenders of last resort to avert any possible problem in access to student loans and thereby provide a nationwide network of back-stop lenders. The Education Department established a Lender of Last Resort plan back in 1998 when some lenders were indicating they might withdraw from the Government Guaranteed Loan program. But the Department did not need to have that program implemented at that time because of a change in the law. Our interest this morning is whether or not that plan has been updated, whether or not meetings have been held with the guaranty agencies, whether or not the agreements that were arrived at at that time have again been updated for today's contingencies, and whether or not all lines of operations are in fact clear should the Secretary need to impose that authority to continue access to loans for students and families.

In addition, the Federal Direct Loan program is available to schools that wish to temporarily or permanently use the program to ensure that students can have access to student loans. The Direct Loan program does not rely on private credit markets for raising capital to originate these new loans. One of the questions we asked the Secretary and will ask again this morning is whether or not efforts have been made to have schools preregister should they decide to use the Direct Lending program. Apparently, it is a very small difference from the information they provide for the FFELP program and then whether or not they are certified, so that they can use that program should they decide to use that as an alternative. And I would hope that what we would see is that we are not waiting for a problem to develop because we have been forewarned. This committee's staff and the chairman have held a number of meetings with lenders from all sectors of the student loan community. The Democratic leadership has held a series of meetings over the last several months with economists and the investment community from Wall Street. And all of them are talking about the unprecedented nature of the credit markets that we have seen and that has spilled over into the municipal bond market,

that has spilled over obviously into both the commercial and residential real estate market and to some extent in the student loan market as institutions have tried to recapitalize their ability to make future loans.

That is why we are here today, to make sure that if that recapitalization does not take place in the volume that is necessary, that we have the ability to step in and to make sure that these students do not miss classes that are necessary for their graduation or for their majors; that they do not miss semesters or quarters that will then cause them to have to borrow more money to go on and finish their degrees. In today's loan-dependent educational environment, it turns out that time is money for families and for students. And we should be in the position of being able to assure those students and their families that they will not have to spend additional time because we failed to make the preparations to provide those loans in the event that the private markets are unable to do so.

Having said that, again, we have received many assurances, both privately and publicly, that the private markets believe they will be able to continue to do that. Some have raised the issue that they think there may very well be a gap. They do not suggest that it is a terribly sizable gap, but it is a gap that must be filled in a seamless fashion so that students and families are not required to go into deeper debt because we couldn't sort out the bureaucratic operations between our institutions of higher education, students and families, and the Federal programs that are designed essentially for this exact situation, whatever that cause may be.

And with that, I would like to recognize the senior Republican on the committee, Mr. McKeon, for his opening statement.

[The statement of Mr. Miller follows:]

**Prepared Statement of Hon. George Miller, Chairman, House Committee on Education and Labor**

Good Morning. Welcome to today's hearing on "Ensuring the Availability of Federal Student Loans."

For months now, the worsening economic downturn has made life more difficult for America's workers and their families.

First the foreclosure signs began sprouting up in front yards. Then, in increasing numbers, the pink slips started arriving. Many American workers are wondering if they will be able to hold onto their homes and their jobs in the months ahead.

In Congress, our priority has been to help get the economy back on track, help workers keep their jobs, and help families keep their homes.

Last month, Democrats and Republicans in Congress acted to give the economy a shot in the arm and deliver relief to families in need right now.

By putting money into the hands of low- and middle-income families who will spend it quickly, the bipartisan stimulus package we enacted will inject demand back into the economy.

This downturn had its roots in the subprime mortgage crisis, which has led to a significant tightening in the credit markets. As a result, what began as a challenge for home loan borrowers has also become a challenge for other borrowers, like those with credit card debt.

Recognizing that the financial markets are not functioning well, the Federal Reserve has recently announced that it has made $400 billion available to financial institutions to help provide liquidity for, and restore confidence in, the general credit markets.

Recently, some federal student loan lenders have encountered difficulties in accessing the capital market to finance their lending activity. While these disruptions have had an impact on some lenders, they so far have not negatively affected students' ability to access federal loans.

Some lenders have expressed concern about their ability to continue to make loans through the Federal Family Education Loan Program, but others are antici-

pating increasing their student loan business in response to changes in the FFELP marketplace, in particular depository institutions like JP Morgan Chase who have publicly indicated their desire to increase market share.

While I am hopeful that overall credit market conditions will soon improve, it is only prudent to prepare now to ensure that stress in the credit markets does not prevent students and parents from continuing to have uninterrupted, timely access to federal college loans.

As we have seen far too often, shocks in the credit and financial markets come as a surprise, leaving those affected little time to react.

In the unlikely event that stress in the credit market leads a significant number of lenders to substantially reduce their activity in FFELP, federal law already includes tools that the U.S. Education Secretary can use to ensure that all eligible students continue to have uninterrupted and timely access to federal student loans. We will examine these tools in today's hearing.

Specifically, the Higher Education Act allows the Secretary to designate the 35 guaranty agencies around the country as "lenders of last resort".

Under existing law, these guaranty agencies are obligated to serve as lenders of last resort to avert any possible problem in access to student loans, thereby providing a nationwide network of backstop lenders.

The Education Department had established a lender-of-last-resort plan in 1998, when some lenders were indicating that they might withdraw from the guaranteed loan program. The Department never needed to implement the plan.

In addition, the federal Direct Loan program is available to schools that wish to temporarily or permanently use the program to ensure students can access federal student loans. The Direct Loan program does not rely on private credit markets for raising capital to originate new loans.

I look forward to hearing from Secretary Spellings about her Department's preparations for implementing a lender-of-last-resort plan and for helping schools enroll in the Direct Loan program in the unlikely event that such steps are necessary.

Having plans in place and operational now will help ensure that all stakeholders, including colleges and the federal government, can respond to any potential loan access problems with the least possible delay for students, families, and schools.

And knowing that the Education Department is fully prepared to act if necessary will reassure students and families that they will continue to have uninterrupted access to federal student loans.

One of the key priorities for this Committee has been to make college more affordable and accessible for every qualified student who wants to attend.

Last year, we took a truly historic step towards this goal by providing more than $20 billion in financial assistance to low- and middle-income students and families over the next five years.

Among other things, this legislation will reduce the cost of federal college loans for student and parent borrowers.

I am confident that, with proper planning by the federal government, students and parents will continue to be able to access these low-cost loans.

I'd like to thank all of our witnesses for joining us today, and I look forward to your testimony.

Thank you.

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Mr. MCKEON. Thank you, Mr. Chairman.

Good morning. Good morning, Madam Secretary.

Thank you, Mr. Chairman, for holding this hearing to examine a looming challenge for our Nation's higher education system. We are here today to examine how to ensure the availability of Federal student loans. By virtue of holding this hearing, we are acknowledging the potential risk to loan availability that has developed in recent months. I consider it a positive sign that Members on both sides of the aisle recognize these challenges. I only hope we can come together in the same way to find solutions.

There are several factors that have contributed to the current student loan uncertainty: deteriorating confidence and reduced investor demand in the capital markets due to the subprime mortgage meltdown; increased financing costs; the possibility of higher defaults because of overall economic weakness; and the real and

perceived impact of the subsidy cuts imposed just a few months ago.

I want to be clear on this point, while the program cuts imposed last fall are not the cause of the current market instability, they are certainly playing a role. There are real questions about whether loan providers will continue to participate in the Federal loan program as a result of the cuts enacted in the College Cost Reduction and Access Act. Those cuts, when coupled with the current instability in the current markets, may create the perfect storm where loan providers may find themselves unable to finance student loans.

The Federal Family Education Loan program has used innovation to absorb various program cuts and policy changes over the years. However, there is a point at which no further cuts can be absorbed, and in all likelihood, we will not know with certainty that we have reached that point until it is too late. Our intention today is not to sound a false alarm. Each of us hopes that the predictions of a loan crisis never come to pass.

Part of our purpose today is to identify solutions so that we are prepared whether or not the situation grows worse. Members on both sides of the aisle have joined together in an effort to engage Federal regulators immediately. Letters have been sent to the Secretary of Education, who we will hear from shortly. They have been sent to the Secretary of the Treasury. And a letter will soon be sent to the Chairman of the Federal Reserve.

Our goal in engaging the various Federal agencies now is to try to prevent any harm to the Nation's college students before it occurs. We are trying to avoid a situation similar to the current mortgage crisis by intervening before students are left without options. Concerns have been raised by members on and off this Committee because the problem is much larger than just this Committee. Any real solution needs to be a result of extensive discussion with parties who are experts in the financial market arena, and I am glad we have an expert from Wall Street here today.

I offered an amendment during the recent consideration of reforms to the Higher Education Act. With that amendment, I proposed a Sense of Congress that these same Federal agencies should be closely monitoring the situation in the student loan credit markets and that they should act quickly to notify Congress in the event of a problem so that we could act quickly. It was disappointing that my amendment was not made in order. I am afraid we sent a signal then that we do not care. However, by holding this hearing today we are sending a powerful signal of our commitment to a robust and healthy student loan system that continues to deliver tens of billions in federally backed loans that help students achieve their college dreams.

Today's hearing is on a topic of utmost importance, and so I will keep my remarks brief. I simply want to note that our purpose here is not partisan. It should not be an effort to favor one loan program over another. Nor should it be used to point the finger of blame. We must look to the future and keep our focus squarely on what will be best for students and families who are pursuing higher education and the benefits and personal enrichment that come with it.

Once again, I want to thank Chairman Miller for holding this hearing. I want to thank Secretary Spellings for being here, as well as our panel of expert witnesses, and I yield back.

[The statement of Mr. McKeon follows:]

**Prepared Statement of Hon. Howard P. "Buck" McKeon, Senior Republican, Committee on Education and Labor**

Good morning. I want to begin by thanking you, Chairman Miller, for holding this hearing to examine a looming challenge for our nation's higher education system.

We are here today to examine how to ensure the availability of federal student loans. By virtue of holding this hearing, we are acknowledging the potential risk to loan availability that has developed in recent months. I consider it a positive sign that members on both sides of the aisle recognize these challenges. I only hope we can come together in the same way to find solutions.

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Once again, I want to thank Chairman Miller for holding this hearing. I want to thank Secretary Spellings for being here, as well as our panel of expert witnesses. I yield back.

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Chairman MILLER. Thank you.

Madam Secretary, welcome to the Committee. You are no stranger to this committee. But just for our audience, I would say that Margaret Spellings is the U.S. Secretary of Education.

And we welcome your appearance this morning.

Prior to being Secretary of Education she was Assistant for Domestic Policy to President George W. Bush. And prior to that she was a Senior Advisor to then Governor George W. Bush with responsibilities for education reform in the State of Texas.

We look forward to your testimony and thank you for your cooperation and our conversations and your making your staff available to our Committee to talk about how we put this in place.

**STATEMENT OF HON. MARGARET SPELLINGS, SECRETARY, U.S. DEPARTMENT OF EDUCATION**

Secretary SPELLINGS. Thank you very much, Mr. Chairman. Thank you for inviting me here today.

Thank you, Congressman McKeon, as well.

I welcome the opportunity to discuss what the Department is doing to ensure that students and families can access and afford higher education. I share your concern and I appreciate your vigilance on this issue. Many of you have written to me regarding your concerns. Today I am responding to you in a letter. Much of my response will also be captured in my remarks.

First of all, let me assure you and especially students and families that Federal student aid will continue to be available. As your recent letter noted, Mr. Chairman, disruptions in the private lending market have so far not negatively affected students' ability to access student loans. That is what we are seeing also.

Student loans constitute a more than $400 billion enterprise involving multiple Federal agencies, guaranty agencies and secondary markets. Federal loans and other Federal aid comprise one piece of this sector, about 26 percent in dollar terms. In student terms, more than 10 million of 18 million college students receive financial aid from my Department. The two sources of Stafford loans are the Direct Loan program and the Federal Family Education Loan program, what we all called FFELP. More than 2,000 originating lenders participate in FFELP.

As recent media reports have noted a small number of these lenders have reduced their participation or stopped originating new loans. As you know, these actions are largely a result of broader stress across credit markets and the economy as a whole. Even in the limited cases where lenders have reduced participation in FFELP, other lenders have stepped in to meet student needs.

My Department is in regular contact with schools. In our extensive outreach, no institutions have indicated that any eligible student has been denied access to Federal loans. And earlier this week, the Consumer Bankers Association reaffirmed that banks plan to continue making both guaranteed and private loans in the coming school year.

Of course, we all understand the anxiety that students and families experience when they hear news accounts suggesting that Federal student loans could be at risk. We also understand that credit markets are under stress and conditions may change rapidly. For that reason, the Department of Education, in consultation with

other offices and agencies across the executive branch, including the Domestic Policy Council, the National Economic Council at the White House and the Treasury Department, is taking the following steps.

First, we are monitoring the situation closely, just as you are doing. We are examining market conditions on a daily basis and working with the lending community, including the many stakeholders involved in Federal aid to assess any potential impact on students. This monitoring will provide us with information on how best to proceed. For example, we are tracking the volume of loan originations for both FFELP and the Direct Loan program against previous years. We know that originations will peak, as they always do, in July and August before the school year starts. If origination trends shift, we will be prepared to act. We are also tracking inquiries daily into the Direct Loan program to be prepared for any significant shift in loan volume between the programs. Again, rest assured that we will be ready should such a shift occur.

Second, we are engaging our customers, students, families and institutions, by helping them understand all of their options. Recently we sent letters to college presidents and financial aid officers to assure them of the continued availability of Federal loans and to ask for their help tracking developments, including any reduction of lender participation. In cases where the institutions are relying heavily on a single lender that chooses to reduce participation in FFELP, we will help identify other lending options.

Third, we are reviewing the options and tools available should the situation warrant their use. For example, some have suggested shifting more of the Federal aid volume to the Direct Loan program. Whether to participate in the FFELP or Direct Loan programs is a choice that schools make. The administration continues to support having two strong Federal student loan programs. Currently 850 schools already authorized to make direct loans have chosen to remain with FFELP as their primary program. We stand ready to support them in whatever choices they make now and in the future. We are also reviewing Lender of Last Resort provisions that ensure eligible students in the FFELP program can access loans if they are turned down by lenders. Currently, the FFELP and Direct Loan programs continue to meet student needs. Lender of Last Resort provisions remain available, and we are closely reviewing the readiness of guaranty agencies to play their role. Private loans can also be an important resource for students and families. However, many who use private loans haven't fully exhausted their Federal aid options. To inform them about these, we have created materials like this Federal Aid First brochure, a user-friendly guidance on how to apply for and receive aid.

It is also worth noting that concerns about the availability of student loans are related to anxiety about the growing cost of attendance. To pay for higher education families must rely upon numerous funding sources while navigating a Byzantine and often burdensome financial aid system. It is like a family having to buy a new car every year for each student in the family with different terms and conditions for each one each year. Working together we can help ease these families' burdens.

Already we have worked together to dramatically increase Pell Grants. We have achieved the largest increase in budget authority in 30 years, and the President has once again asked to increase the maximum annual award in his 2009 budget to $4,800 per year. As early as 2006, my Commission on the Future of Higher Education called for streamlining the financial aid system by addressing the interrelated issues of cost, financing and consumer information. As you work to reauthorize the Higher Education Act, I hope we can take this opportunity to simplify the system and make it more responsive to students and families. Postsecondary education grows more important by the day in our global knowledge economy. Times of economic uncertainty are all the more reason that Americans will look to higher education to acquire new skills and knowledge. Together we can help more of them do so.

Federal student loans are an important part of this effort, and the steps my Department is taking will help ensure that they remain available. Market conditions are dynamic, not static. As you said in your letter, Mr. Chairman, while we expect that overall credit market conditions will soon improve, it is only prudent to prepare now to ensure that these conditions do not negatively impact students. In the coming weeks and months I look forward to working with you to help students continue to access and afford the invaluable opportunities of higher education.

And Mr. Chairman, here today with me is Larry Warder, who leads our Federal student aid operation, as well as my General Counsel, Kent Talbert.

[The statement of Secretary Spellings follows:]

**Prepared Statement of Hon. Margaret Spellings, Secretary, U.S. Department of Education**

Thank you for inviting me here today. I welcome the opportunity to discuss what the Department is doing to ensure that students and families can access and afford higher education. I share your concern and appreciate your vigilance on this issue.

First of all, let me assure you, and especially students and families, that Federal student aid will continue to be available. As your recent letter noted, Mr. Chairman, disruptions in the private lending market have "so far not negatively affected students' ability to access federal loans." That's what we're seeing also.

Student loans are more than a 400 billion dollar enterprise, involving multiple federal agencies, guaranty agencies, and secondary markets.

Federal loans and other federal aid comprise one piece of this sector. Of eighteen million college students, more than ten million receive financial aid from my Department.

The two sources of Stafford loans are the Direct Loan program and the Federal Family Education Loan program—what we call FFEL. More than 2,000 originating lenders participate in FFEL. As recent media reports have noted, a small number of these lenders have reduced their participation or stopped originating new loans.

As you know, these actions are largely a result of broader stress across credit markets and the economy as a whole. Even in the cases where lenders have reduced participation in FFEL, other lenders have stepped in to meet student needs. My Department is in regular contact with schools. In our extensive outreach, no institutions have notified us that any eligible student has been denied access to federal loans. And earlier this week, the Consumer Bankers Association reaffirmed that banks plan to continue making both guaranteed and private loans.

Of course, we all understand the anxiety that students and families experience when they hear news accounts suggesting that federal student loans could be at risk. We also understand that credit markets are under stress, and conditions may change rapidly.

For that reason the Department of Education—in consultation with other offices and agencies across the executive branch such as the Domestic Policy Council, the National Economic Council, and the Treasury—is taking the following steps:

First, we are monitoring the situation closely—just as you are doing. We're examining market conditions on a daily basis and working with the lending community, including the many stakeholders involved in federal aid, to assess any potential impact on students.

This first step will provide us with information on how best to proceed. For example, we are tracking the volume of loan originations for both FFEL and the Direct Loan program against previous years. We know that originations will peak, as they always do, in July and August before the school year starts. If origination trends shift, we will be prepared to act.

We are also tracking inquiries daily into the Direct Loan program to be prepared for any significant shift in loan volume between the programs. Again, rest assured that we will be ready should such a shift occur.

Second, we're engaging our customers—students, families, and institutions—by helping them understand all their options. Recently, we sent letters to college presidents and financial aid officers to assure them of the continued availability of federal loans, and to ask for their help tracking developments, including any reduction of lender participation at their schools.

In cases where the institutions are relying heavily on a single lender that chooses to reduce participation in FFEL, we have actually communicated with these institutions to ensure that their students will continue to be served, be this either a single lender or other new lenders.

Third, we're reviewing the options and tools available should the situation warrant their use. For example, some are suggesting that we shift more of the federal aid volume to the Direct Loan program. Whether to participate in the FFEL or Direct Loan programs are choices that schools make. The Administration continues to support having two strong Federal student loan programs. Currently, 850 schools already authorized to make Direct Loans have chosen to remain with FFEL as their primary program. We stand ready to support them in whatever choices they make, now and in the future.

Congress included the Lender of Last Resort provisions in the Higher Education Act to provide a way for the Federal Government to ensure, should the need arise, that students and families can continue to access FFEL loans. These provisions are called "last resort" for a good reason—they're the final option for eligible students unable to access federal loans. At present, the FFEL and Direct Loan programs continue to meet student needs. Lender of Last Resort provisions remain available, and guarantee agencies are already using their authorities as needed.

Private loans can also be an important resource for students and families. However, many who use private loans haven't exhausted their federal aid. To inform them of the more affordable Federal options, we've created materials like this Federal Aid First brochure—user-friendly guides on how to apply for and receive Federal aid.

As early as 2006, my Commission on the Future of Higher Education called for streamlining the entire financial aid system by addressing the interrelated issues of cost, financing and consumer information. As you work to reauthorize the Higher Education Act, I hope you will take this opportunity to simplify the current system, which is burdensome and complex, and make it more responsive to students and families.

Already, we've worked together to dramatically increase Pell Grants, to address the needs of 5.8 million low-income students. We achieved the largest increase in budget authority in 30 years, and the President has once again asked to increase the maximum annual award in his 2009 budget, to $4,800 per year.

Postsecondary education grows more important by the day, and ever more necessary in our global knowledge economy. Times of economic uncertainty are all the more reason that Americans will look to higher education to acquire new skills and knowledge. Together, we can help more of them do so.

Federal student loans are an important part of this effort, and the steps my Department is taking will help ensure that they remain available. Market conditions are dynamic, not static. As you said in your letter, Mr. Chairman, while "we expect that overall credit market conditions will soon improve * * * it is only prudent to prepare now to ensure that these conditions do not negatively impact students * * *" I look forward to working with you to ensure that students can continue to access and afford the invaluable opportunities of higher education.

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Chairman MILLER. Thank you very much.

Welcome, Mr. Warder, also.

Under a previous agreement, Mr. McKeon and I will both be allowed to exceed our initial 5 minutes but not by more than 10 minutes. So hopefully it will be somewhere between 7 and 8 minutes to ask more extensive questions on these two programs.

I think we all agree that we hope that the FFELP program stays in place and it meets the demand and it sorts out the difficulties that have been imposed upon the various lenders by the rather dramatic shift in the credit markets. But I would like to run through the Lender of Last Resort program with you because that is where we have had some experience in the sense of preparation back in 1998 when we thought that some lenders might leave the field. Then-Secretary Riley put in place a program and an agreement with the guaranty agencies for those loans to be made if necessary.

And maybe, Mr. Warder, you can tell me, has that agreement been reviewed, and has that agreement been updated with the guaranty agencies?

**STATEMENT OF LAWRENCE A. WARDER, CHIEF FINANCIAL OFFICER, U.S. DEPARTMENT OF EDUCATION**

Mr. WARDER. Yes. We have asked all of the agencies—we have gone out to all of the 35 guaranty agencies and asked them to submit to us what their current plans are. We have reviewed those, and we are in the process of issuing guidelines on how you would implement Lender of Last Resort in the instance that it is needed. So those guidelines will be going out in the coming week, along with any suggestions on how to improve the agreements that they currently have. Again, this has been a rarely used program over the last few years, so what we are doing is updating it, making sure they are consistent, in the best interest of both the tax payers and the students.

Chairman MILLER. And you expect those guidelines to be in place when?

Mr. WARDER. We are sending them out next week, so we would expect them to be in place in the near future.

Chairman MILLER. And then how will you determine whether they are operational or not?

Mr. WARDER. We will go out and meet with the GAs either collectively or individually to review the program and make sure that they have the financing capability to in fact act as Lender of Last Resort or have another lender who can do that.

Chairman MILLER. Well, Lender of Last Resort, as I understand the program, is the Secretary in that case?

Mr. WARDER. Actually, the Lender of Last Resort in the current environment, since there is no longer a national, the Lender of Last Resort is the guaranty agency. Our relationship is with them.

Chairman MILLER. But they turn to you to be capitalized?

Mr. WARDER. Generally, no. That would be only in an absolute last resort.

Chairman MILLER. That is what I want to talk about.

Mr. WARDER. Their obligation is to have the financing capability in place and use it.

Chairman MILLER. As I understand the 1998 agreement, that agreement was in place, so then the Secretary, if necessary, turned

to the Treasury to fund them so that they could make those loans. That is not your understanding?

Mr. WARDER. Let me ask our general counsel who can probably respond to that better than I.

**STATEMENT OF KENT D. TALBERT, GENERAL COUNSEL, U.S. DEPARTMENT OF EDUCATION**

Mr. TALBERT. Mr. Chairman, as I understand the 1998 plan that the prior administration had, it had a list of eligible lenders, entities that would be able to make loans of last resort should the need arise. But, again, it is the guaranty agencies and then eligible lenders if the guaranty agencies are not providing Lender of Last Resort loans who make the loans available.

Chairman MILLER. But the guaranty agencies, as I understand the 1998 agreement, turn to, if necessary for capitalization to make those loans, turn to the Secretary of Education who then turns to the Treasury.

Mr. TALBERT. Certainly the Lender of Last Resort statute provides for advances, that advances can be made should the need arise when certain criteria are met.

Chairman MILLER. We are working on the scenario where the need arises. What I want to know from you is if you understand that that is your legal authority and you have the ability to do that?

Mr. TALBERT. Yes, we understand the statute, yes.

Chairman MILLER. And you have the ability to do that?

Mr. TALBERT. Certainly, the administration has the ability to make——

Chairman MILLER. Have you road tested it? Have you turned to the Treasury and said, if we have to make a demand on you for $100 million or for $5 billion, will we be able to have that demand met so that we can give it to the guaranty agencies to make these loans if that is the shortfall that exists at that time?

Mr. TALBERT. Certainly, again, the authority is——

Chairman MILLER. I know the authority exists, sir. I am asking whether or not if you have asked the operational question? We had a lot of authority going into Katrina, but nobody asked whether or not we could do it, whether we could do it in the sense—could we physically get people out of there, people there, water, all the rest of it? I am asking you, operationally, have you sat down with the Treasury Department and asked them, if we turn to you and make a demand on short notice, because most of the things that have taken place around the credit markets have come to a surprise to everyone, including those involved, could you do this?

Mr. TALBERT. We are having ongoing discussions within the administration, including——

Chairman MILLER. So you have not received an answer to that question of whether or not, if you make a demand, that demand can be met?

Mr. TALBERT. Again, Mr. Chairman, we are having ongoing discussions in the administration about this particular matter.

Chairman MILLER. Well, I hope you are not standing in 8 feet of water and a lot of students around you looking for relief and you are having ongoing discussions. The purpose of this hearing is to

push those discussions so an agreement and an operational plan is arrived at.

Mr. TALBERT. Well, again, our position now is that, again, no borrower has been unable to obtain loans.

Chairman MILLER. I understand that. This isn't about the environment.

Madam Secretary, we have been through this. This isn't about a well operated system. We hope that the FFELP program is in place. We have been notified by lenders that they will not participate. We have been notified by lenders that they hope they will be able to continue to participate. We have been notified by lenders they expect to participate but are not quite sure how long. And all of them have said they suggested there would be a gap. Rather than operating on the theory that nobody has notified you, what will you do in July and August if in fact the gap appears, and how seamless will it be?

Secretary SPELLINGS. As you know, Mr. Chairman, the 35 guaranty agencies exist. We have reached out to them. We are looking at their plans. They have been uneven. They need to be made current. That is the guidance that is going to them next week. We will evaluate their capacity to seek financing should that case occur, and obviously, if not, we are the lender of very last resort.

Chairman MILLER. Have you spoken to the Treasury about that?

Secretary SPELLINGS. We have; my staff has. I have spoken with Secretary Paulson once, and I will be meeting with him next week. I can assure you I will be asking him that very question, very specifically. I think at the moment, we are getting a beat on the capacity of the guaranty agencies who are now updating their plans accordingly. Yes, I will ask him that.

Chairman MILLER. And do you need to arrive at an agreement with those agencies?

Mr. TALBERT. Well, the agencies have their plans and procedures in place now. Again, we are reviewing those to make sure that they are adequate and good to go.

Chairman MILLER. Let me just suggest that if you look at the 1998 agreement, there was just a modest little modification for that agreement with the law. Today a borrower has to run around and find out that two lenders have turned that borrower down. A suggestion was made in 1998 that an institution could stand in the shoes of that borrower and make that decision and turn to the Federal Government and therefore be able to invoke the Lender of Last Resort. A modest change, but could be very important in terms of being able to answer the question from a student or family, will the money be here so I can start school this coming semester? It is those kinds—you know, a number of these agencies, they prepared for this. A number of the people who were there in 1998 are still here today. And somehow, I think, rather than sort of this arms distance length, you ought to get in the same room and say, what are the agreements we need so this plan will be operational if you pick up that phone at 3:00 in the morning and have to call one of them. That is the best I can come up with. I want to know they say, we are ready to go.

Secretary SPELLINGS. As you know, none of that was needed in 1998.

Chairman MILLER. I know that. That was because it was solved by a change in the law. We can change the law until hell comes home, and it is not going to unfreeze the credit markets from this Committee.

Secretary SPELLINGS. We will be ready.

Chairman MILLER. And then with respect to the direct lender program. My understanding is that essentially, if you are making—if you are eligible for Pell Grants as an institution, you are eligible for the DL program, but you still have to sort of make application and be certified?

Secretary SPELLINGS. That's correct. And 850 institutions, if you will, sort of have that franchise.

Chairman MILLER. Right. And they sort of leave it over there in reserve, and they continue in the FFELP program?

Secretary SPELLINGS. That is correct.

Chairman MILLER. I am just asking whether it would be prudent or not to suggest that other institutions may want to be precertified. Again, if they don't need it, they can leave it over there, continue in the FFELP program and go on about their business. Because, again, you know, schools have deadlines for applications, for receiving funds and all the rest of this and very small glitches can be leveraged into major disruptions in students' lives. I have suggested to the institutions in my area that is what they may want to consider; that, one, they clearly understand what the arrangement is with their guaranty agency, and they clearly understand if they want, how they get certified and eligible for the Direct Lending program, and then we hope that this gap will not exist.

Secretary SPELLINGS. I think they do understand that. There is, and frankly the private sector has led the way on establishing inoperability and protocols. We are updating our system in the Department so that those transitions can be made if necessary. I would also say, and I know you are well aware, that institutions, were they to turn to Direct Loan, obviously that places additional sort of an administrative burden on them that now you know lives in the marketplace. And so I think they are evaluating those issues now. They make those choices, and we are ready to support them in whatever choice they make.

Chairman MILLER. Also in our discussions with some of the guaranty agencies they are very concerned about whether or not this system will—they believe this should be prepared on an electronic basis; that if the Lender of Last Resort programs are necessary, that they reflect an electronic processing environment. And, again, I don't know if you have run the traps, operationally, whether or not you can do that or not, because you may have to handle a significant volume of loans in a very short period of time, and that is not going to work absent an electronic environment.

Secretary SPELLINGS. As I understand it, there is increasing interoperability across this sector, including our work at the Department of Education.

Chairman MILLER. Mr. Warder, is that your understanding?

Mr. WARDER. Yes, it is. The institutions that are FFELP institutions generally can switch from lender to lender very easily. We are in the process of putting in place, and this will take a few months, the ability to tap into that same network so we can look like a

lender just like the other FFELP lenders. Currently, today, we have a process that can get somebody ready and certified within one to two weeks. Then it is how long, how sophisticated is the institution in implementing whatever changes they need to make in order to access direct loans.

Chairman MILLER. So, again, if they make that demand in July, you say it takes about two weeks?

Mr. WARDER. It is two weeks to get the authorization. Then it is whatever their implementation time frame is to get their own procedures and processes in place.

Chairman MILLER. I think I will stick with my advice to my institutions; they ought to consider doing that now since you are talking about several months to be electronically able to do this. That sounds like June. And if they make a demand, it is two weeks for the application and then for whatever negotiations. I would suggest they may want to do it now.

I thank you, and my time has expired.

Mr. MCKEON.

Mr. MCKEON. Thank you, Mr. Chairman.

Chairman MILLER. Could we just have the counsel state your full name for the record? I am sorry.

Mr. TALBERT. Kent Talbert.

Chairman MILLER. Thank you.

Mr. MCKEON. Thank you, Mr. Chairman.

I came to Congress in 1992, the same time as President Clinton. One of the things he campaigned on was Direct Lending, and that was quickly put into place. And a lot of the schools jumped into Direct Lending, and I think they got up to 30, 35 percent of the loan volume. And then, over the years, we did the reauthorization in 1998, and one of the things we did was adjust the interest rate. And one of the concerns I had was that FFELP lenders would be dropping out of the program, and that has happened. And then we tried to have a level playing field. I know Mr. Kildee and I agreed on that. The Secretary at the time, the administration, didn't, and there were things done during that administration that pushed people into Direct Lending.

But over the years, the market has reacted, and FFELP had about 80 percent of the business and Direct Lending about 20. We had problems with Direct Lending back when they had to shut the program down because they couldn't keep up with demand. And we have seen this kind of a problem over the years. In 1995, we cut the FFELP lenders $18 billion out of their subsidies. More lenders dropped out of the program. And then, last year, the same thing was done, another $18 billion. And now we are looking at, gee, maybe we have a problem. I think it doesn't take a lot to realize that if you cut the subsidies to the point where lenders no longer can make a profit, why should they stay in the business. There are other things they can lend.

One thing that is helping us right now ironically is, because of the problem in the housing market and the lack of funds, there is less interest for the banks to move in to making home loans, and so there is still some interest in staying with making student loans. But the loan consolidation companies have gone out of that business. FFELP lenders I know have laid off a lot of people because

they are getting out of the business. I am hearing from schools, it is like there is a disconnect.

Madam Secretary, you say that you are not hearing from schools that there is a problem. I am hearing from schools that there is a problem. And I am hearing from schools that they have been told that lenders will not make loans to their students, especially in the proprietary area; that the cost of direct or of private loans is a lot more to students than the federally backed loans. And so, where we passed this bill to cut the cost of college, we have actually increased what students are going to be paying in interest for their loans. Have you heard from any proprietary schools that they have been told that their students will not be able to get loans?

Secretary SPELLINGS. Well, as I said, Congressman, we have reached out to every institution. We have heard some limited cases of contraction where they have been able to readily find another lender in those cases to date.

Mr. MCKEON. Well, okay. I am glad we are having this hearing because I think a few months from now, we are going to look back on it and say, you know, where did all this stuff come from? I think the question that the chairman just asked, can you come up with $1 million or $5 million, we are talking $60 billion that we are expecting the FFELP lenders to make this year this summer and fall for students to get into school. And if that has to all of a sudden be found, I just see a very serious problem coming down the pike. And I hope this hearing is soon enough that there is a wake-up call that you are able to work together with the Treasury and are able to come up with substantial funds that students that don't have a clue what is coming down the pike when they go in to meet with their Federal financial aid officer, that you are able to make sure that there is sufficient money in the pipeline that either through FFELP or through Direct Lending, they will not have a glitch and that the interest rate will not be such that it drives up the cost of their education. Do you feel confident that this will be the case?

Secretary SPELLINGS. We are taking every step possible to ensure that that is the case. As I said, we have reached out. We have plans. We are meeting regularly with Treasury. As I said, I am going to be meeting with Secretary Paulson next week and, you know, will provide additional assurances and ask them those very questions. We are still in the fact-finding mode about what the capacity, what the potential gaps might be. As you are also aware, lenders have likewise stepped forward and said that they do intend to and will make FFELP loans this year.

Mr. MCKEON. It is my understanding that you are talking and have talked to Secretary Paulson and other officials within the administration to help you monitor the credit markets. Can you tell me about those conversations and whether officials outside of the Department of Education are concerned about students' access to lending?

Secretary SPELLINGS. Well, clearly, Congressman, we are talking very regularly, daily with our colleagues within the administration, obviously, about all these provisions. And likewise, as you are reaching out to the community more broadly; guaranty agencies, institutions, banks, lenders, all of those affected. So, yes, we are monitoring regularly.

Mr. MCKEON. Mr. Chairman, thank you.

I will yield.

Chairman MILLER. Thank you.

Mr. ANDREWS.

Mr. ANDREWS. Thank you, Mr. Chairman.

Thank you, Madam Secretary, for working with us to solve what I hope is a hypothetical problem that never comes. But the virus that spread throughout the credit markets in this country counsels us to pay attention. And I know you are. And I wanted to walk through with you some of the Chairman's questions about the Lender of Last Resort program. I hope we don't need it. But if we do, there is a couple of mechanical steps that I want to see if you would be willing to be supportive of. I know you have the authority. I think we have established that. The question is whether you would be willing to embrace certain principles to get this up and running, should it be needed.

First, how about school-based qualification rather than student-based? The existing procedure is that a student has to demonstrate that he or she has been turned down by at least two lenders. What do you think of the idea of having some threshold, or if we hit that threshold, that the whole school is eligible and every student at that school is eligible for a loan under the Lender of Last Resort program; do you support that?

Secretary SPELLINGS. Well, again, we are engaging with the guaranty agencies about those sorts of thing. As you may or may not know, various lenders and schools have different types of approaches for different types of students. So, for undergraduates, they may seek one route; for graduate students, they may seek another. And so I don't think we know enough yet to answer that question.

Mr. ANDREWS. When do you think you might know? Because here is what I am worried about, you get a student from—a first in a family to go to college, and it is July 15th, and she goes to a bank and fills out these papers and the bank says, sorry, we are not making any more student loans. There is a very high probability she just stops, because she is not someone who is used to dealing with bureaucracy and these kind of things, she just stops and doesn't go to school. I just think, as happened in 1998, that some metric ought to be established that says, if this happens to a certain critical mass of people, then let us switch to a deal where the school can apply for LLR participation and everybody at the school is eligible if they fit the other criteria. I would urge you to do that and think that through. Second is, how about electronic loan processing? If we are mailing documents back and forth on August 25th, there is going to be a lot of people who don't go to school. Not to mention, by the way, the technical and career schools which have a revolving calendar. This is already happening at some of the schools that are trying to enroll people for courses that start April 1st or March 25th. It isn't just with courses with a traditional calendar that starts up around Labor Day. How many of the guaranty agencies and schools are ready to process these loans in an electronic processing context? Do we know? How many of the agencies are ready to do that?

Mr. WARDER. Are you asking about the GAs, are they prepared to do it?

Mr. ANDREWS. The guaranty agencies, yes.

Mr. WARDER. I don't know. We are looking at their capabilities around Lender of Last Resort as we speak.

Mr. ANDREWS. When do you think we would know? I think there are 36 guaranty agencies, you said, right? I think the optimal situation would be that all 36 could originate, process and fund loans electronically to the extent possible. If that—do you agree that that is a standard?

Mr. WARDER. I would agree that is an objective. In fact, the schools through their normal FFELP program or DL program do process them electronically. However, we do need to look and see how well prepared the GAs are on the LLR——

Mr. ANDREWS. That is right, because, frankly, the schools being able to do it is only half the battle, and that is 20 percent of the schools, right, that are in the Direct Lending program? So, again, if we are using 1965 technology to send these documents back and forth, and we have a huge spike in loan volume, it isn't going to happen.

The third thing I would urge you to consider is permission for the guaranty agencies to sell these loans, these LLR loans, if a marketplace exists, to be able to sell those loans in that marketplace to be liquid again. My sense is they already have the legal authority to do that and for purposes of keeping them viable. What is your position on that, that if they have a bundle of LLR loans, we think they have the legal authority to turn around and sell them to cash them out? Do you, and if so, would you support that?

Mr. TALBERT. There is no prohibition on selling the loans. Now, if advances are made, the guaranty agency would need to hold onto the loans because the Department can demand that they be assigned back to the Department.

Mr. ANDREWS. I would urge you to rethink that, because as long as the Federal taxpayer interest is protected I think increasing liquidity in the system is a huge value. The following thing, I would say, is I would urge you to take a look at the testimony from the witness from the University of Maryland who is about to come up, the financial aid director. And she lays out the case of a first-year residential student that falls $3,600 short of what she is going to need, even after she maxes out on the Federal programs. I would urge you to think about how we are going to capitalize PLUS and private gap loans in this environment should that eventuality occur as I think it already is.

Secretary SPELLINGS. Clearly that is the sort of thing that we are describing in the new materials that we are making available. Congressman, one thing that strikes me about your various questions is the need for us to, and certainly I commit this to Chairman Miller, to communicate regularly with you about what we find as we survey guaranty agencies as to their electronic capacity or lack thereof.

Mr. ANDREWS. I see my time is up. I certainly hope that is the case. I think you heard from both the Chairman and Mr. McKeon a bipartisan interest in working this problem through, not assign-

ing blame, but avoiding the problem and trying to solve whatever comes along. Thank you very much.

Chairman MILLER. Mr. Keller.

Mr. KELLER. Thank you, Mr. Chairman.

And I am very concerned about the impact of the credit market on the student loan programs and on the ability of students to gain access to college.

Madam Secretary, let me ask you a couple of questions relating to the FFELP and the direct loan program. As you know, four out of five schools use the FFELP program rather than the direct loan program, I believe, because there are many advantages that the FFELP program has in terms of the ability of these lenders to offer low origination fees, lower rates, better repayment benefits, if they so choose. On the other hand, there are many good advocates in government for the direct loan program as well.

In your testimony, you said that you have been tracking inquiries daily into the direct loan program. Have you seen any increase in the number of inquiries from schools considering switching to the direct loan program?

Secretary SPELLINGS. A small number, Congressman.

Mr. KELLER. You mention that there are 850 schools authorized to make direct loans, but they have chose to remain with the FFELP program. You are not suggesting, are you, that those schools who are authorized to be in the direct loan program but currently use FFELP should switch to the direct loan program are you?

Secretary SPELLINGS. Absolutely not. And I do think it is important to—you know, obviously, financing is not the core mission of higher ed institutions. And they enjoy having the capacity of service and other features that benefit students, you know, live in the private sector as opposed to having to create those structures internally themselves.

Mr. KELLER. We have heard about the Lender of Last Resort program. Just by the way that that is set up with the Federal Government having to turn around and pay the guarantors to make the loans, while there certainly seems to be a benefit of having that last safety net there, isn't it also true that if we were to go to the Lender of Last Resort model, it would in fact be even more costlier for the taxpayers than either the FFELP program or the Direct Lending program?

Secretary SPELLINGS. That is correct, as we would be liable for 100 percent of the default. We are also working with OMB to calculate the potential costs of those issues at various levels should that occur, and we will share that with you as we do.

Mr. KELLER. Now, as we look at this potential crisis there doesn't seem to be yet a crisis from your testimony, it seemed that there are different levels of exposure right now in the student lending world. For example, and I want to ask your opinion, if you were at a school that has the FFELP program or direct loan program, pretty good graduation rates, low default rates, chances are you are going to be in good shape in getting your federally backed student loan this year; correct?

Secretary SPELLINGS. I would think that would generally be true, yes. Large public institutions, that sort of thing.

Mr. KELLER. Now, let us go to the other extreme. Let us say that you were at a private career college that has a pretty high tuition and your federally backed student loan doesn't cover everything, so you have to go out and get a private loan to cover the difference. If you have——

Secretary SPELLINGS. As is currently the case, of course.

Mr. KELLER. Right. And obviously, in that scenario, they look at your credit score, or your mom and dad's credit score; there is no Federal backing. And if you happen to be at a school with a high default rate and a low graduation rate and you or your parents don't have a pretty good credit score, you are exposed in terms of your ability to get a competitive low interest loan; is that right?

Secretary SPELLINGS. Well, obviously, there is a guaranty agency that surrounds that type of institution. And as you know, there is no credit check when that Lender of Last Resort provision is invoked. So, ultimately, that student gets financing.

Mr. KELLER. Right. But at a higher rate just because the market determines the financing. And if money is tight and your credit score is low, inevitably those students in this type of credit crunch are going to be faced with higher student loan interest rates?

Secretary SPELLINGS. In the private sector, in the private market, yes.

Mr. KELLER. Correct. From your conversations with the Treasury, Secretary Paulson, and other officials within the administration, what is your level of optimism that, at least with respect to the next 12 months, the existing federally student backed program will be sound moving forward for young people in America?

Secretary SPELLINGS. My level of optimism is high, and my level of hope is higher, obviously. But even notwithstanding that we are going to be fully prepared to react to whatever situation confronts us. Obviously, it is completely in the context of the overall economic picture. And you know, as such, student loans will be implicated if situations worsen generally. But you know, I think we are taking all necessary steps, not only in this arena but in the administration more broadly, to stem that.

Mr. KELLER. Thank you, Madam Secretary.

My time is expired.

Chairman MILLER. Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman.

Madam Secretary, let me follow up on that because I was a little confused by the answer. Whatever school you go to, if you apply for a loan, I thought you indicated that no one so far has been denied a loan that is looking for a loan. Is that right?

Secretary SPELLINGS. To our knowledge, that is correct.

Mr. SCOTT. And wherever you go, the interest rate you will pay on that guaranteed loan will be the same whether it is a fancy school or not?

Secretary SPELLINGS. What Congressman Keller was asking about, I believe, was loans in the private sector. Certainly that is true up to the limits within the Federal financial aid system. Obviously, private loans, interest rates, can and do vary.

Mr. SCOTT. But up to that limit, credit worthiness is not a factor?

Secretary SPELLINGS. That is correct.

Mr. SCOTT. Traditionally student college assistance has been in the form of loans, Pell Grants and work study. It seems to me that we are leaning much more heavily on loans than we traditionally have. Can you comment on the direction we are going in and whether that is a healthy direction?

Secretary SPELLINGS. Well, as you know, together we have worked hard to raise that Pell Grant. And I agree with you; I mean, with tuition rising as rapidly as it is, we are having a hard time keeping up with those increases. And I think the system, while we are obviously talking about a critical symptom today and certainly at this time, there are certainly bigger issues throughout the entirety of the system about affordability and transparency and levels of aid and so on and so forth. But, yes, I think we have to continue to work to increase need-based aid, and we have.

Mr. SCOTT. How many students are participating in the income contingent repayment plan?

Secretary SPELLINGS. How many students?

Mr. WARDER. I don't know. We will have to get you that. I am not sure how many are.

Mr. SCOTT. Many?

Mr. WARDER. It is a reasonable number, but I couldn't even give you an estimated percentage.

Mr. SCOTT. What about the loan forgiveness plan which passed, several bills that allow loan forgiveness if you go into certain professions? Have those plans shown any evidence of encouraging students to get into those fields?

Secretary SPELLINGS. We are in the process of implementing those. As you know, they are fairly recently passed and are in the rule-writing process. And we can certainly get you the numbers of people who get teacher loan forgiveness and some of the things that are on the books. I don't have that off the top of my head, but we can get that for you.

Mr. SCOTT. I yield.

Mr. MCKEON. Back to the question you were asking and the question Mr. Keller was asking. If a student has used all their help, the Pell grant, and they get the full Federal financial aid loan, and they still need a gap loan, the Lender of Last Resort doesn't kick in there. That is a private loan, and they would be—and if they can't get that loan, they are out. And that is one of the students that I am really concerned about.

Mr. SCOTT. I reclaim my time. If you have used up all your Pell grant, all your loan eligibility, you are on your own to find the rest of the money. Your credit worthiness and everything else comes into play.

Secretary SPELLINGS. That's right.

Mr. SCOTT. That is why we need to make sure that the Pell grants cover more of a portion and work study covers more of a portion so that the loan amount will in fact cover their full education.

Secretary SPELLINGS. What we are engaged in today is a discussion around 26 percent of the full financing of education. That is our discussion. The other 24 percent of those resources come from States, from families, from home equity loans, often credit cards,

on and on. We are talking about this slice of the pie that we have jurisdiction over.

Mr. SCOTT. We measure the school's effectiveness in loan repayment on a default rate. If a school has a high default rate, they may become ineligible for participation in the student loan program; is that right? If you exceed the default rate, is that right?

Mr. WARDER. Well, there is a threshold on default rates on the 2-year cohort default rate that if they exceed it, the schools are out of the program.

Mr. SCOTT. It seems to me that that is a poor measure of how well a school is doing in having the payments repaid, because it seems to be more a function of who you admitted than how hard you are working to get the payments back. If you had a first generation college student, low income, someone with marginal grades, you are discouraging colleges from opening their doors and giving people a second chance and limiting them to those who are credit worthy when they walk in. Is there some other measure that we could use other than a default rate?

Mr. WARDER. Well, we do use a number of measures, that being one of them. Certainly they need to be accredited and have an appropriate amount of their financing coming from other than Federal sources. So there are multiple measures.

Mr. SCOTT. But the default rate, if you exceed the default rate, you are out, period?

Mr. WARDER. But very few have exceeded the default rate. With a change to a 3-year default rate, that may be different. But currently, there has been very few suspended for default rate.

Secretary SPELLINGS. Congressman also, as you know, through the accreditation process, issues of financial management, financial solvency, are absolutely part of that gateway. That is what gets you a proxy of eligibility for Title IV aid in the first place. And so I think that is probably more appropriate for the accreditation discussion or is implicated more in the accreditation discussion than in this arena.

Chairman MILLER. The gentleman's time has expired.

Mr. Hare?

Mr. HARE. Thank you, Mr. Chairman.

Welcome, Madam Secretary.

You stated in your testimony that you and your department are monitoring the situation, the student loan industry, and you are in contact with schools and students, et cetera. By these actions, you say you will be prepared to act, should there be a shift in the origination trends.

Could you maybe explain a little bit more about what you mean here? In other words, what would be the first steps you would take if you see a shift?

Secretary SPELLINGS. Well, as you know, it would be largely fact-specific. But I think the tools that are available to us I have described as support for the Direct Loan program should it become necessary, use of the Lender of Last Resort provisions should that become necessary. Those are obviously the main two tools that are available to us, the Department of Education, should such a situation arise.

Mr. HARE. Are there any other resources or authority that we, the Congress, can provide you to yield quicker and more aggressive responses should we find ourselves in a major-league crisis here?

Secretary SPELLINGS. We believe that the statute that you all have described is adequate to respond to this situation. But I reserve the right to come back and tell you otherwise in the near term if it is not. But we believe, as you indicated in your opening statement, Mr. Miller, that it is, that we do have the tools available.

Mr. HARE. And then just lastly, you said, in addition to the Lender of Last Resort in the Higher Ed Act, are there other measures that you are aware of, that are authorized in the law, that allow you to respond to a certain crisis that you may encounter in the student loan industry?

Secretary SPELLINGS. Are there other tools available besides the ones I described?

Mr. HARE. Right.

Secretary SPELLINGS. Well, I know some have suggested things that reflect in the credit market more broadly that are issues that Treasury would have jurisdiction over with respect to the Federal Home Loan Bank or the Federal Reserve or other mechanisms like that, but not that are within the discrete discretion of the Department of Education.

Mr. HARE. And lastly, my colleague Mr. Andrews's suggestions that he laid out—I thought every one of them made perfect sense. And I think they would go a long way toward helping, should we have a problem here. And who knows whether we are going to have one or not, but I think it is better—you know, the old adage is, better to be safe than sorry.

So I would hope that you take those into consideration, because I think Mr. Andrews is right on point with each one of these three that he brought up specifically, you know, to you as recommendations. And I would hope that you take a look at them and maybe get back with us and see if those can't be implemented. I think they make a lot of sense and go a long way toward helping if we have a problem here.

Secretary SPELLINGS. May I say—and I fully expect to do this—that, as we gather information about capacity and gaps and so forth as we interface with these guaranty agencies and the like, this guidance we are issuing next week and so forth, I look forward to sharing this. This is very much an iterative, organic, dynamic situation. And we will be in close communication between now and August, I assure you, Mr. Chairman.

Mr. HARE. If I could, I would like to yield the balance of my time to my friend, Mr. Andrews.

Mr. ANDREWS. I appreciate it. I just wanted to ask one quick follow-up question. I thank my friend for his compliment and appreciate his help.

Madam Secretary, do you think some sort of Federal guarantee facility is necessary for the gap loan situation that Mr. McKeon talked about, that others have raised? The person who is $2,000 or $3,000 short under the Federal programs, has read your brochure, but is maxed out? How do we attract capital into the system to help that person who is in the subprime market borrow money?

Secretary SPELLINGS. You mean essentially a guarantee of private loans that would work like that? You could certainly——

Mr. ANDREWS. I am asking what you think the strategy would be to help attract capital to that market for those gap loans. What would work?

Secretary SPELLINGS. Well, I would say, you know, I think that we have a great deal of work to do, frankly, on the cost side before we talk about, you know, additional supports for private lenders. I think we have not done enough to make transparency about cost, to make information available about how to maximize Federal aid. I mean, lots of kids with private loans still have money on the table federally. So I think we have some work to do.

Mr. ANDREWS. But many do not. But many do not. I appreciate——

Chairman MILLER. If the gentleman would yield just for a second?

Mr. ANDREWS. Yes.

Chairman MILLER. Just to the last point the Secretary made, I think we have looked at one and maybe a couple of studies that have suggested about 50 percent of the students have not maximized their access——

Mr. ANDREWS. Right.

Chairman MILLER [continuing]. To government loans, but they are under intense marketing pressure sometimes, and they turn to the private loans prematurely.

Mr. ANDREWS. Right.

Chairman MILLER. And, of course, then they find out that they could be in trouble.

So we are not quite clear yet. I mean, clearly there are students who need that private loan to fill that gap, to make that tuition and cost. But there is a good number of students and families who have turned to private loans without maximizing the Federal program. And that is a matter of educating people, to make sure that they do that.

Secretary SPELLINGS. And simplification. I mean, I think one of the things that you can see from this chart——

Chairman MILLER. That is in the conference committee.

Secretary SPELLINGS [continuing]. Is this is a very difficult system to interface with. And I think we could do a lot on the simplification side that would help students maximize the rate.

Chairman MILLER. It has been suggested it is easier if these students and families went to the World Bank, they would be more likely to get a loan, than if they accessed this system of banking.

Secretary SPELLINGS. I sometimes say it is like we are trying to keep them out.

Chairman MILLER. With Mr. McKeon's help, we are going to sort that out in the conference committee.

Mr. Davis?

Mr. DAVIS OF TENNESSEE. Thank you, Madam Secretary, and thank you for understanding the pressure that students and families are under.

One of the things that we need to do, as they are looking for money to pay for higher education, is understand that we need to do everything we can to lower the cost of higher education. Because

one of the things I see is, as we put more money in, the cost of higher education goes up. And then there is a need to put more money in, and then the cost of higher education goes up. And that's where families are really feeling it, back in my district in east Tennessee. And thank you for understanding that.

And, with that, I would like to yield the remainder of my time to Mr. McKeon.

Mr. MCKEON. I thank the gentleman for yielding.

Madam Secretary, can you describe how you plan to monitor the market beyond waiting for responses from college presidents and their financial aid offices?

Secretary SPELLINGS. Larry can speak to that, as well.

But, as I said, we have written every single one of them and asked for a response if they saw any problems. We have heard from about 60 to date.

Mr. MCKEON. You have heard from 60?

Mr. WARDER. Yes.

Mr. MCKEON. Out of?

Secretary SPELLINGS. More than 4,100.

Mr. WARDER. We are doing some other monitoring, as well. Obviously, we read the newspapers, as you do, and when we hear of a lender discussing either withdrawing, reducing or whatever their FFEL support, we immediately contact all of those schools that have 50 percent or more of their volume with that lender. And every time we have run into one of those, we have contacted them and they have been able to line up another FFEL lender. So we continue to monitor those situations. Any wind we get, we are on the phone with the schools to see what their intent is.

Also, we monitor every month the originations that occur, both in FFEL and in DL. And so far there has been—I mean, it looks just like every other year. But we are watching our data, as well.

Mr. MCKEON. In your statement, you state that the Department supports both the FFEL program and the Direct Loan program. Haven't we already failed the FFEL program if you find that the Lender of Last Resort provision needs to be implemented?

Secretary SPELLINGS. Well, I don't believe so, Congressman. I think that this industry is—and, obviously, people with far greater expertise, like Chairman Bernanke, have asserted this also—this is a viable sector of the financial market. Obviously, it is impacted by, you know, broader things in the credit market. But we look forward to that being, sort of, stabilized over time and that it will continue to be and has been a very financially viable sector.

Mr. MCKEON. Do you have any reports or information as to how many people have been laid off as a result of the—you know, working in the FFEL program, that have been laid off because of companies pulling back?

Secretary SPELLINGS. I don't have a total number. I, too, have seen anecdotal reports of that, but I do not a have a total number in the industry.

Mr. MCKEON. The last report we have is it is over 2,000 people. And those people were working in making those loans. And if they are not now working in that, I am sure there has been a pull-back that—you know, where you are monitoring loans being made right

now. We are not in the season of loans being made. It would be interesting to see——

Secretary SPELLINGS. Right.

Mr. MCKEON [continuing]. What starts happening by June, July. And then if we find out there is a serious problem in August, it is too late.

It is my understanding that the Pennsylvania Higher Education Assistance Authority, PHEAA, has stopped making loans in Pennsylvania.

Secretary SPELLINGS. Originating.

Mr. MCKEON. Originating. And do you know of an example of how the Department is assisting institutions within the State to find other lenders? Do you know how successful they are being?

Secretary SPELLINGS. There are about 40-some-odd or so that have—17 institutions are new entrants. In other words, they are just now becoming eligible for Title IV aid and so forth; they are new to the program. There are some other double-digit number, 40 or so, I believe—do you want to speak to that, Larry?

Mr. WARDER. Again, PHEAA being another lender, we have contacted all of the schools that have 50 percent or more of their origination volume with PHEAA. And, so far, they have continued to be able to find another FFEL lender, or, in the case of one large institution, they switched to DL. They already had the DL authorization, and they have announced that they are going to switch to DL. And that will be a fairly large increase for DL.

Mr. MCKEON. I guess that is the ultimate goal anyway, for some of us.

Chairman MILLER. Not for you.

Mr. MCKEON. Not for me. I am not included in that "us."

Secretary SPELLINGS. Neither am I.

Mr. MCKEON. Thank you very much.

Secretary SPELLINGS. Thank you, Congressman.

Chairman MILLER. Thank you.

Mr. Bishop?

Mr. BISHOP OF NEW YORK. Thank you, Mr. Chairman.

First, let me ask unanimous consent that I can enter into the record a statement on this subject from Dr. Phillip Day, the president of NASFAA.

Chairman MILLER. Without objection.

Mr. BISHOP OF NEW YORK. Thank you.

[The information follows:]

**Statement of Dr. Philip Day**

**President and CEO**

**National Association of Student Financial Aid Administrators**

**U.S House of Representatives**

**Committee on Education and Labor**

**Hearing on Ensuring the Availability of Federal Student Loans**

**March 14, 2008**

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Mr. Chairman and Members of the Committee. On behalf of the National Association of Student Financial Aid Administrators (NASFAA), I am pleased to offer this statement. I am Dr. Philip Day, President and CEO of NASFAA. Formed over forty years ago, NASFAA represents student financial aid administrators at some 3,000 postsecondary institutions across the nation.

Our association illustrates the diversity of our higher education enterprise with members from private and public institutions, community colleges, four-year schools, proprietary schools, and graduate/professional institutions. At these schools, NASFAA represents approximately 12,000 financial aid professionals who are dedicated to helping families apply for and receive the funds they need to send their students to college. Each year, financial aid professionals help more than 16 million students receive funding for postsecondary education. Given the complexity of the state, federal, and institutional aid programs, it is necessary to have someone with that kind of expertise guiding students and families through the process.

I want to begin by complementing the work of you, Mr. Chairman, and the members of the committee for all you have accomplished providing additional numbers of students with opportunities to gain a postsecondary education. The College Cost Reduction and Access Act (CCRAA) is magnificent testimony to your commitment to the Title IV programs.

Just to name two examples of that commitment found in the CCRAA are the substantial increases in the Pell Grant maximum award and establishment of the Teach Grant program. These two programs illustrate your devotion to serving the needs of students expeditiously and creatively. We applaud mandatory spending increases for the Pell Grant. We likewise welcome inventive programs like the TEACH Grant that seek to help meet the unique needs of specific students.

The Committee on Education and Labor will soon complete reauthorization of the Higher Education Act. H.R. 4137, The College Opportunity and Affordability Act, also contributes to your record of success. H.R. 4137 authorizes a $9,000 Pell Grant maximum award, provides loan forgiveness for service in areas of national need, increases loan limits and provides for additional public service loan cancellations for Perkins loan borrowers, and simplifies the FAFSA. The bill brings transparency and accountability to the student loan process by specifically addressing issues from the recent loan scandals. We are especially pleased by Title X of the House bill that applies FFELP reforms to private educational loans.

Again, Mr. Chairman, I thank you and the Committee for your accomplishments in the 110th Congress that will help so many students and families. This is a record of success you can justly be proud of and NASFAA salutes your efforts and contributions to making college affordable and making the student aid process more effective and simpler.

Today's hearing is timely. On Tuesday I wrote to my membership. Here is what I told them.

> Alarming reports in the media about disruptions in the credit markets that are affecting student loans have many families worried that they won't be able to get student loans in the

fall. I have assured financial aid administrators, students, and parents that the likelihood of disruptions in federal student loans remains low.

To date NASFAA is not aware of any student being denied a federal student loan due to market conditions.

Some news reports fail to distinguish between federal and private student loans, but understanding the difference between the two is crucial. The vast majority of student borrowers use federal student loans. Federal student loans - like Perkins, Stafford, and PLUS loans -- that are backed by the federal government. Federal student loans are not dependent on borrowers' credit scores; the repayment terms and conditions are specified by federal law, and are better than private loans. Interest rates and fees on federal student loans will not increase. Low-cost federal student loans are still available. Even in instances where student loan providers have suspended their loan programs, other loan providers have stepped in to fill any vacancies.

A far smaller group of students rely on private student loans or other forms of consumer financing like home equity loans. These students turn to private loans if they cannot cover their cost of attendance with federal, state, and institutional financial aid -- including federal loans. Like other consumer loans affected by the subprime mortgage meltdown, private student loans will be costlier for some borrowers at some institutions this academic year. However, students and parents should only use private education loans as a last resort. Before borrowing private loans, students should exhaust all the federal, state and institutional financial aid available to them.

NASFAA understands that what is happening in the student loan market is fluid. The liquidity that exists today to continue funding federal student loans could be gone tomorrow if the markets worsen. Of particular concern are the liquidity problems that state and non-profit secondary market lenders face. Unlike traditional banks, nonprofit state agencies that operate secondary markets raise capital through bond auctions. As you know, these bond markets are currently frozen and they are unable to raise enough money to provide additional liquidity to other lenders. Their inability to raise capital serves as another warning sign that all is not well in the student loan markets.

Nonprofit loan providers fill an important niche in the student loan market and often times purposefully target low-cost loans to specific, underserved populations or offer specific loan benefits to particular populations such as future teachers, nurses and military veterans. These are the students and families that are often-times overlooked by other lenders and the types of students the federal student aid programs were created to help. A total departure by state agencies and nonprofit lenders would be detrimental to students and parents, especially those attending schools that lenders have deemed "at-risk." While federal student loans remain available for the majority of students, we are hearing reports that some loan providers are shying away from schools with students who need low-cost loans the most. It is conceivable that if the nonprofit lenders are unable to offer loans this fall the students who would be harmed most would be from our community colleges, proprietary schools, and other urban-based public and private institutions. Special measures may be necessary to assist these nonprofit, state-based

organizations to ensure their continued presence in the federal student loan market.

If conditions worsen to the point where the availability of federal student loans becomes threatened, the following alternatives are in place.

- The Department of Education could utilize the "Lender of Last Resort" provision, where federally-designated guaranty agencies would line up lenders to continue making loans to students or would be given funds directly from the government to disburse to students.

- A school that has a problem accessing federal student loans through the Federal Family Education Loan Program (FFELP) can join the federal government's Direct Student Loan program (DL), where the government lends the money directly to students without using any lender.

To ensure a smooth financial transition into college this next academic year, NASFAA advises students and families to apply for financial aid early by using the Free Application for Federal Student Aid (FAFSA). We are telling students to work closely with their school's financial aid office to complete the financial aid process – including applying for federal student loans - as early as possible. Students and parents with any questions or doubts about the availability of student loans or other forms of financial aid should always contact their financial aid office for specific information.

There are also things that legislators and the Department can do to ensure there are no disruptions in federal student loans. Schools who are interested in moving to the Direct Loan Program face many system conversion costs. Given that we are only five months away from the beginning of fall term, other schools question whether there is enough time to move into the Direct Loan Program. We advocate the Department take extraordinary steps to ensure that such a transition is as seamless as possible for schools.

Lender-of-last resort provisions should also be examined to ensure that students have direct access to federal loan funds without some of the roadblocks currently stipulated in regulation. For example, current ED regulations allow guarantors to require proof that a borrower has been denied a loan by as many as two lenders before a lender-of-last resort loan can be approved. This requirement requires diligence and an understanding of the student loan process, which puts an undue burden on the student borrower. Another example is the requirement that a guaranty agency act on the borrower's lender-of-last resort application within 60-days. Certainly, we believe most agencies would not take 60-days. But, the lender-of-last resort statutory and regulatory provisions should be reexamined in light of their possible widespread use.

As we move forward, NASFAA will continue to research and identify workable solutions that should be taken to ensure the continued availability of federal student loans.

Let me say a word or two about private educational loans. Approximately 25 percent of student loan volume comes from these educational loans. Those loans are made when a student's financial aid package (Federal grants, work/study, and loans, plus any state aid or school-based grants) is insufficient to cover their educational costs.

Our members are telling us that private educational loans are changing for some borrowers. The credit score needed to secure these loans are rising. Interest rates and origination fees are also increasing. Access to private loans could be a problem in certain sectors of higher education, such as proprietary schools, community colleges and urban-based colleges and universities, all of whom serve a disproportionately large number of high-risk, economically disadvantaged students. Correspondingly, and to the best of our knowledge, most traditional colleges are not experiencing access problems.

We believe that as a nation we should do everything in our power to decrease the need and growing dependence on private student loans. To that end, NASFAA recommends fully funding the Pell Grant Program to prevent the neediest students from having to borrow at all. We also believe the campus-based programs should be funded at sufficient levels to help middle-income families. Finally, we believe the federal student loan programs' annual and aggregate loan limits should be significantly increased to reduce reliance on private educational loan borrowing and keep borrowers within the safety of the federal loan programs. In order to accomplish that objective **we want to strongly express our support for Senator Kennedy's amendment offered on the Budget Resolution to modify the provision establishing a Higher Education Reserve Fund to allow for increases in the federal loan program's loan limits.**

These actions will go a long way towards fulfilling the promises made by the Higher Education Act when it was signed into law nearly 43 years ago.

When President Johnson signed the Higher Education Act into law on November 8, 1965, he said, "[W]hen you look into the faces of your students and your children and your grandchildren, tell them that you were there when it began. Tell them that a promise has been made to them. Tell them that the leadership of your country believes it is the obligation of your Nation to provide and permit and assist every child born in these borders to receive all the education that he can take… And tell them that we have opened the road and we have pulled the gates down and the way is open, and we expect them to travel it. And when we meet back here again a few years from now, there will be many more than the 1,300 and the 5,500 that will be here seeking and receiving the knowledge that is an absolute necessity if we are to maintain our freedom in a highly competitive world."

My members know all too well how far away we are from achieving the goal of equal opportunity to postsecondary education for low- and middle-income families and students. But we are getting closer. Our focus, first and foremost, must be on meeting the financial needs of the disadvantaged. I know we all share President Johnson's commitment to make his dream our nation's reality.

I pledge NASFAA's support – along with the 12,000 aid administrators that I represent - to assist you, Mr. Chairman, and to assist your colleagues as you address the issues involved in today's hearing. You must cajole when cajoling is necessary. You must act when action is necessary. I do not believe the American people will tolerate a meltdown in access to federal student loans similar to what they're seeing in other credit markets.



The good news is that tools are available at your and the Department of Education's disposal to deal with any disruptions in federal student loans, no matter how unlikely that may be. While the law has solutions in place, it is critical that we test these solutions and prepare for the worst case scenario today. In addition, new tools can be created as needed to meet specific needs that the Congress believes are appropriate to prevent problems. Waiting until the height of the lending season in July through September is not an option. All parties should meet to discuss solutions and develop plans to prevent a possible train wreck this fall. We look forward to working with you to ensure all our citizens credit needs are met in paying for a postsecondary education.

Mr. BISHOP OF NEW YORK. Madam Secretary, thank you very much for coming this morning and for working with us to try to address this issue.

I can't escape the feeling that we are working at cross-purposes with this issue. And let me be specific. We are concerned about some difficulty in accessing student loans, which is just a piece, as you said, of the overall student financial aid delivery system. And yet, while we are concerned about that, the administration's budget proposal to Congress eliminates SEOG and recalls the Perkins Student Loan Revolving Fund. SEOG is about $750 million a year; Perkins Loan Revolving Fund is around $700 million a year.

And so I am perplexed as to why, when we have this concern that students will be able to access funds to finance their education, that we are taking things away from them that they have relied upon for years and have worked reasonably well.

And so, whenever I have asked this question before, the response is, "Well, we want to put our resources into Pell." But when you come to an individual student, that just doesn't work. I mean, the Pell grant maximum is $4,731. We are going to increase it to $4,800. So a fully needy student will get $69 more from Pell, but could easily lose $1,500 in SEOG, could easily lose $1,500 in Perkins. We are going to drive that student more to private loans, which we all agree are something that we need to shape up.

So just tell me what the logic is of an elimination of round numbers, a billion and a half, of campus-based money that we have relied upon for years and students have relied upon for years, and we are replacing it with $69 in Pell. So explain to me how that helps the student access his or her educational school of choice.

Secretary SPELLINGS. Part of this, Congressman, as you said, is an effort to strive to increase Pell.

However, the other part of this is that we must simplify the system. To have 16 different programs with different types of eligibilities for students, for institutions, and to try to navigate that kind of system makes it very difficult for students to interface—in fact, so difficult, that many do not access.

Mr. BISHOP OF NEW YORK. Respectfully, respectfully, let me just say the campus-based system is a very straightforward system that requires no separate application on the part of the student. The student submits one form, the very same form that they need to file to get Pell, the very same form that they need to file to get other forms of financial aid. But the financial aid officer at their school has available to them a pool of resources that they can then use.

So it seems to me that if the goal is to simplify, what we are really doing is erecting obstacles. And I just don't understand—and I know you share the goal of helping students realize their dreams. But how is it, if we are going to take a billion and a half dollars out of the system, even if we think the system is complicated, how does that help students access their dreams?

Secretary SPELLINGS. Well, as you said, you know, by increasing Pell—now, obviously there is not a one-to-one correlation about particular students who may lose aid and so forth. But I think in a general construct that Pell ought to be greatly enhanced—we

have asked for it to be again this year—and that we ought to simplify the system.

Mr. BISHOP OF NEW YORK. And we are enhancing Pell. And we are on a path to get us to $5,400.

Let me focus just on Perkins, if I may. Clearly, we are having this hearing because we are concerned about whether or not FFEL program will remain as available for students as has historically been the case.

If, in fact, FFEL does become less available, would the Department rethink its position on Perkins? Would you say, here is a perfectly reasonable alternative, low-cost alternative, infrastructure is in place to deliver it, all we need to do is allow schools to continue to maintain and administer and award from the revolving loan fund? Would the Department rethink their position on their desire to eliminate Perkins?

Secretary SPELLINGS. Well, Congressman, obviously, these all have budgetary implications. And, you know, obviously, we work with OMB as we take positions over time. That is a theoretical question that is not before us and, obviously, not mine alone to make.

Mr. BISHOP OF NEW YORK. I understand that, and I thank you. I see my time has expired. Thank you, Mr. Chairman.

Chairman MILLER. Mr. Loebsack?

Mr. LOEBSACK. Thank you, Mr. Chairman.

I don't have any questions as such. I just want to make a couple of comments, following up, at least in one case, on Mr. Davis's comment.

First, I was a long-time college teacher at a small college in Iowa, at Cornell College. And also I am someone who came from pretty humble backgrounds, grew up in poverty, and was able to access what was then the National Defense Student Loan Program—3 percent interest, had grants, that sort of thing as well. And without all that financial aid, I clearly wouldn't be here, sitting in Congress, as a freshman member from Iowa.

So I am very concerned about some of the issues also that were just brought up by my friend from New York. But as someone who was on an institution's faculty, I want to caution everyone that, while I am very concerned, obviously, about student access to college and achieving the American dream, I also want to make sure that we don't go too far in terms of, sort of, blaming the institutions themselves too. And I realize that is not what you are doing. But, being on this committee, I have heard a number of comments since I have been here about institutions. Obviously, some institutions have raised their costs pretty exorbitantly beyond inflation, what have you, but I am not at all convinced that in every instance they are to blame, necessarily, for that, because I think they have very good reasons for increasing their costs.

So I just want to, sort of, lay that on the table now for the public record, that I think sometimes some members of this committee, and perhaps both sides of the aisle, have unfairly bashed institutions since I have been here. And I hope no one here takes any offense at that comment. But at any rate, I think that is important to keep in mind.

On the other side, as far as the students are concerned at least, I have great concerns also about the administration's budget. I just want to echo what my friend from New York has said. I simply don't understand how it is the case that, in the name of simplification, that reducing assistance for potentially millions of students makes any sense. It makes absolutely no sense to me.

I realize that is sort of a broader issue that is not directly related to what we are talking about today, but I do think it is really important to keep that in mind, sort of, the bigger picture here. You know, we are talking about loans today, but I think we need always to keep in mind, sort of, the larger goal, which is for students to have access to higher education so they can achieve the American dream, so they can do things that I have been able to do, fortunate enough to do in this country.

And I just want to caution the administration when it comes to making cuts in the Perkins program or any other cuts in the name of simplification or whatever the case may be, especially if it is, in fact, going to reduce access to higher education, which I think, in fact, is what will happen.

So I don't really have any questions as such. If you want to comment on the comments I just made, that is fine.

Thank you.

Secretary SPELLINGS. I would like to react to the first part of your observation. And that is, I agree with you, I think we do have sort of a mixed bag of understanding of what the costs, you know—why do we have such rapidly rising tuition costs. And I think this area begs out for more information and more transparency and more understanding by our publics.

And, again, I think, as you all debate the Higher Education Act, that is certainly something that can be, I think, really addressed in that context.

Mr. LOEBSACK. I yield back the rest of my time, Mr. Chairman. Thank you.

Chairman MILLER. Thank you.

Mr. Tierney?

Mr. TIERNEY. Thank you, Mr. Chairman.

Thank you, Madam Secretary, for being here with us this morning.

I would like to just clarify a couple of points, if I could. One is you talked a little bit earlier about the Lender of Last Resort situation and the possible need of going to the Secretary of the Treasury to discuss with them, in the ultimate last resort, whether there would be resources available for the Department of Education to work with guarantors.

Have you had that conversation with the Secretary? And if you have, in what detail?

Secretary SPELLINGS. We are having conversations about all available options.

Mr. TIERNEY. Specifically that option have you discussed with the Secretary?

Secretary SPELLINGS. About specific levels of resources?

Mr. TIERNEY. Whether you have had any at all, whether he makes them available, and levels.

Secretary SPELLINGS. I certainly intend to.

Mr. TIERNEY. But you have not yet?

Secretary SPELLINGS. I have not yet. We are in the process of finding out what are our resources, how much do they cost, what is the order of magnitude—fact-gathering before we sit down and reach conclusions.

Mr. TIERNEY. Okay. But you expect to have that conversation with him in the relatively near future?

Secretary SPELLINGS. I do.

Mr. TIERNEY. The other clarification I wish to ask was, in the plan, in 1998, it provided for a school—Mr. Andrews mentioned this earlier—a school that was unable to locate a lender willing to lend to its students to be able to notify the guaranty agencies, certify its students that have been unable to obtain loans, and then being able to work on behalf of the students through the institution, as opposed to requiring each student to run around and get two lenders to refuse them.

Is that something you are actively entertaining?

Secretary SPELLINGS. Issues as it relates to the Lender of Last Resort being implicated?

Mr. TIERNEY. Right.

Secretary SPELLINGS. Well, as I have said, we are looking at, through the guaranty agencies, the various procedures that they have in place and whether they are adequate to be able to respond timely to situations such as that.

Mr. TIERNEY. Okay. And have you contemplated what Representative Andrews mentioned, the fact that instead of having the student, individual students going around and getting two rejections, that it might be something we consider having the institution be able to make a certification to the guarantor and then get the loans for all the students at that school?

Mr. TALBERT. Certainly, Congressman, we are looking at that issue, particularly with respect to the letter that goes out next week to the guaranty agencies. The statute speaks in terms of individual borrowers. But I understand, administratively and so forth, the issues. And we are looking at that for purposes of the guaranty agency letter that goes out next week.

Mr. TIERNEY. And so, are you seriously contemplating this may be a path you want to take?

Mr. TALBERT. We are discussing it. We are having consideration of it. And no final decision has been made yet.

Mr. TIERNEY. All right. Thank you.

Chairman MILLER. Would the gentleman yield?

Mr. TIERNEY. Yes, I will yield.

Chairman MILLER. Just on that point, my understanding was that, in 1998, that arrangement was made. Do you differ with the legal ability to do that?

I know what the statute says, but apparently they reached an agreement where——

Mr. TALBERT. Yes, I mean, we certainly have the letters that you do that went out in 1998, and we also are aware of what the statute says now, which legally seems to say it is a borrower-by-borrower consideration. But, again, looking at the administrative issues and so forth, we certainly have that under consideration.

Chairman MILLER. Okay. Thank you.

Mr. TIERNEY. Yield back.

Chairman MILLER. Thank you.

Mr. Sarbanes?

Mr. SARBANES. Thank you, Mr. Chairman. Thanks for having the hearing.

Thank you to the panel.

Mr. Warder, can you just tell me again, you said, I think, that you have some communication or notice to institutions in instances where 50 percent of the loans are coming from one lender. Can you just go back through that?

Mr. WARDER. Yes. One of the things when we get notification that a lender is either reducing their origination in FFEL or saying they will not participate in the next year, we have the information in our system that lets us know what percentage of loans are made through a FFEL lender at a school. So if they have 50 percent or more of their volume, we immediately reach out to them to assure that they are able to replace that volume.

Mr. SARBANES. And how does the reach-out work? What is it you are——

Mr. WARDER. We call the aid office.

Mr. SARBANES. And what is the discussion?

Mr. WARDER. The discussion is around, "We have heard that your lender is not originating. Is that true with you? And what have you done to replace it? And what other lenders have you gone to?" And they have all said they have been able to replace that volume with another lender.

Mr. SARBANES. I guess I am curious why you would only initiate that with respect to institutions where 50 percent of the loans originate with that lender as opposed to, say, 25. I mean, 50 percent is a pretty high threshold to establish before you reach out to the institutions to make sure that everything is okay.

I am wondering, why is it 50? Is 50 percent an internal protocol that is established? Does it originate someplace in particular?

And could it be moved to, say—I mean, this whole hearing is about trying to get ahead of the curve and see the trends coming early and take preventative steps. So, I guess, I would just imagine that you could move that to, say, 25 percent, again, just to get a little bit ahead of the curve. Maybe you could respond to that.

Mr. WARDER. We could do that. The reason we haven't is that if you picked a 25 percent, for example, it says that the school already has lenders lined up for the other 75 percent or less and that they generally have enough relationships with other lenders that they are probably okay.

We have also asked them, if they are concerned about their capacity, their FFEL capacity, to get in touch with us. So we have also asked all of them to get back to us with any concerns they have about their FFEL origination capacity.

Mr. SARBANES. Fair enough. I guess I would just——

Mr. WARDER. But we are not waiting when it is 50 percent or more.

Mr. SARBANES. Again, I would urge you to have a trigger system or a tickler system that might make you reach out earlier than that. You know, even, again, if 75 percent is in the okay category, the way we have seen this credit tightening happen is it can accel-

erate very, very quickly. And in light of that, I would think you would want to be getting some trends identified faster and be having those conversations even earlier.

In other words, I guess what I am saying is the 75 percent that are, quote, "okay" might—you might wake up tomorrow and find out that there are three lenders in there that yesterday thought they were fine or were going to stay in the business, today have decided to get out of it, and they represent 50 percent, between them, of what that institution is relying on. And now, all of a sudden, you are at 75 percent that are in a precarious position. So I would just urge you to find an earlier trigger point for having the conversations.

Thank you.

Chairman MILLER. Thank you.

Mr. Ehlers?

Mr. EHLERS. Thank you, Mr. Chairman.

I would like to zero in on a specific problem and get away from some of the global issues that have been discussed. The specific problem is that of medical students, particularly medical residents.

I have a communication here from the American Medical Association and from others, and I have a major medical center in my district. It is a major problem for the medical students, particularly the residents who had a certain process for keeping their payments very low while they were residents, because, as you know, they get paid very small amounts and have substantial debts at that point, particularly if they are facing a 7-year residency.

The College Cost Reduction Act of 2007 will, I think, eventually help solve this, but there is a bridging problem. There was a debt-to-income pathway, the so-called 20/220 pathway, which has sort of disappeared. And we need something to bridge that.

I just wonder, is the Department working on this, or do you have an answer prepared?

Secretary SPELLINGS. Yes, Congressman, we have retained this test by regulation through November of this year as a bridge until the new provision becomes fully implementable. At that time I know you are well aware that those payments will be much less than the normal full amount. But we do have a bridge to segue, which is essentially the previous system.

Mr. EHLERS. I hope it is not the bridge to nowhere.

Secretary SPELLINGS. No, sir.

Mr. EHLERS. Is this in effect already?

Secretary SPELLINGS. Yes, we have retained that test by regulation.

Mr. EHLERS. And will that stay in place until——

Secretary SPELLINGS. Until the transition is made, yes.

Mr. EHLERS. So everything is solved, it is all in place?

Secretary SPELLINGS. Yes, sir.

Mr. EHLERS. That is a refreshing answer. Very seldom do I get that answer from the Federal Government.

Thank you very much.

Secretary SPELLINGS. Thank you, Congressman.

Chairman MILLER. Thank you.

Mr. Altmire?

Mr. ALTMIRE. Thank you, Mr. Chairman.

Madam Secretary, nobody, certainly on this committee or even in this Congress, is looking forward to the scenario in the fall where we have hundreds of parents and students calling our office every day who didn't realize that they weren't going to be able to qualify for loans and now can't seek higher education at this time as a result. And we appreciate the fact that you have come in the spirit of helping us avert this problem from the beginning and avoid that happening. So we appreciate you being here.

And then, trying to work through it—I am from Pennsylvania. We have the situation with PHEAA, which Mr. McKeon touched on earlier. And you know what has happened there. We have Penn State University, which has now gone to the Direct Loan program in response to that situation. And in the second panel we are going to have somebody who is going to talk about their experiences from, I believe, Iowa State, and they made the switch.

I am just curious if you had any advice to people in Pennsylvania, specifically. You know, with the largest dominant loan agency now unable to participate, you know, the largest university in the State making the decision to go to the Direct Loan program, I would assume there are going to be others to follow. It really appears that it is pretty unstable ground right now, with regard to student loans in that State.

What advice would you have to students and parents, as far as the stability of the program moving forward and what the expectations will be for parents who have children that are about to go into the higher education system?

Secretary SPELLINGS. Well, as I said, Congressman, we have new material that is timely for the situation that we are in that encourages them to maximize their aid. I would suggest to students and families, particularly as we approach April 1, which is the timing that institutions make acceptances known to students, that they look at these issues early and that they seek those resources as early as they possibly can; don't wait.

Mr. ALTMIRE. Thank you.

And do you think that what has happened in Pennsylvania because of PHEAA being so big and Penn State being a big school, that that is unique compared to what other States in the country are facing? Or would you expect that those problems are going to be similar across the country?

Secretary SPELLINGS. I think it is somewhat unique. I think with Penn State, as you know, they had previously been a Direct Loan institution. They had familiarity with it. And so I think they may have had an acceptance and adapting process that might be more streamlined than others.

Mr. ALTMIRE. Okay. Thank you.

Chairman MILLER. Thank you.

Mr. Payne?

Mr. PAYNE. Thank you very much.

I just have a question regarding—of course we all talk about the high cost of college and loans that students have to take out.

Two questions. One, basically we have a tremendous amount of interest today on the part of young people—there seems to be a new esprit de corps of volunteerism, sort of, a new spirit of wanting

to help in areas that are underserved and in Third World countries.

And one of the big areas that we have is the lack of medical personnel in developing countries, where we have the PEPFAR program that President Bush is very proud of, and we support it tremendously. It works on AIDS and TB and malaria and things of that nature.

And we find that there are students graduating from our medical schools who would like to immediately go to Africa, parts of Asia, or where tuberculosis is very tremendous in Eastern Europe, the new strain of TB, but they have these tremendous loans that they have to be responsible for and, therefore, cannot participate—and even in some of the underserved areas in the United States.

Have you thought in terms of any serious programs that could either defer or offset the immediate loan repayments that are due from these students, in order for them to be able to do programs that are in no-paying or low-paying areas, to help offset the loans?

Secretary SPELLINGS. Well, not internationally, Congressman. As you know, we are in the process of implementing the provisions of CCRAA that speak to loan forgiveness in public service areas here domestically. But I am not aware of discussions about forbearance for people doing international aid work.

Mr. PAYNE. I just spoke to former President of the Senate Frist, who, as you know, does a tremendous amount of that type of work. Yesterday, as a matter of fact, he testified before a committee on child survival and global health. And he, too, probably would think something like that would be helpful.

Sometime I would like to talk to people in your department about that, and also about even expanding what we have available domestically. Because I think that they could do a tremendous amount of good, and for a small amount.

The other question, on a totally different area, we had a hearing of the Historically Black Colleges and Universities yesterday here, and there is a goal with the Department of Defense of a 5 percent set-aside goal for HBCUs. However, believe it or not, there is no mechanism to evaluate or quantify whether the goal is being reached. And I would like to also discuss with your staff about some method. It could be 1 percent, it could be zero, it could be 7 percent—I would doubt the 7 percent—but if there was some mechanism that could be imposed, so that we have some idea.

It is great to have a goal. And, of course, you know, we have to be careful, it is goals; they are not quotas. We never did quotas, even though people took goals and tried to switch it around to say they were quotas. We have goals, but it would be good to see whether there is some way to evaluate whether we have been coming close to the goals.

So I would like to be in touch with your staff on that, too.

Secretary SPELLINGS. Certainly. Thank you.

Mr. PAYNE. Thank you.

Chairman MILLER. Mr. Price?

Mr. PRICE. Thank you, Mr. Chairman. I appreciate the opportunity to ask a few questions.

I want to thank you so much for coming. I apologize for not being here earlier. I know you had an extensive discussion about the

issue of Federal student loans. As I say to my son, "I resemble that remark" now. We have one child who is a senior in high school, and so we are looking at—we have been accepted, thank the Lord, and now we are trying to figure out how to go from there.

I have been able to listen to some of the testimony and some of the questions, and I think that the fundamentals are clear about different philosophies about where the responsibility ought to lie, how much role the Federal Government ought to play. Obviously, the majority party believes the Federal Government ought to play a much greater role. And I think it is important, as we review that philosophy, that there are some consequences, both intended and unintended. And I would like to explore one or two of those.

The FFEL program comprises about 80 percent of loans now. Would you agree that it works relatively well——

Secretary SPELLINGS. Absolutely.

Mr. PRICE [continuing]. And is an appropriate and helpful adjunct for probably millions of students to gain access to higher education?

Secretary SPELLINGS. Absolutely. It is the primary way they do within Federal support.

Mr. PRICE. And I would agree and commend the wonderful work that they are doing to allow for greater opportunity for higher education for so many young people across our Nation. There are those who would say that the Direct Loan program ought to be the only program. And I would ask you, if we were to move rapidly in that direction, how quickly can the Education Department add servicing capacity of the DL program if the volume is increased by 30 or 40 or 50 percent?

Secretary SPELLINGS. We can respond quickly. That level—essentially, we could double our current capacity. But, you know, obviously, as it scales up, we would have to come to you for additional resources, should that materialize. But, at this point, we can approximately double the capacity in the program, should we need to.

But, as you know and as you said, we are strong supporters of both programs. Institutions make those decisions. You know, one of the things I think institutions like best about the FFEL program is, inasmuch as financing is not their core mission, they are able to have those services live in the private sector. Institutions will have to create those services internally, were they to join the Direct Loan program.

Mr. PRICE. I think you would agree, Madam Secretary, that having the FFEL program in place allows for greater choices and opportunities for, again, millions of students.

Secretary SPELLINGS. It does.

Mr. PRICE. If we were to move to a significantly greater degree to the Direct Loan program, that would, of necessity, I suspect, increase the debt. The House and Senate adopted a budget yesterday that has significant increase in deficit and increasing the debt.

Do you have any sense about the implications on the national debt if the DL program were to increase to a large degree?

Secretary SPELLINGS. We are looking at cost implications, not only there but also if we need to invoke the Lender of Last Resort and these 100 percent guarantees. There are cost implications for

the various tools that might be implicated. And certainly, as we develop those figures, we will share them with you.

Mr. PRICE. So, as the Nation clamors for some fiscal responsibility and not increasing deficit and debt, it would be appropriate to continue to hold up the FFEL program as one that is a good option and opportunity for, again, millions of young people across this Nation to gain an education without significantly harming the fiscal——

Secretary SPELLINGS. I believe it is.

Mr. PRICE [continuing]. Status of our Nation. I appreciate that.

As a physician, I also want to tell my good friend that we are working diligently to try to make certain that students can have their loans forgiven if they serve domestically in underserved areas.

Secretary SPELLINGS. Right.

Mr. PRICE. And we have large numbers of those, as you well know.

With my remaining time, I am pleased to yield to my good friend, Mr. Ehlers.

Mr. EHLERS. I thank the gentleman for yielding.

I just wanted to follow up with my earlier question. My always-competent and ever-ready assistant assures me that the income-contingent repayment program that you are setting up is a substantial disadvantage for medical residents compared to the 20/220 pathway.

And, as you know, we worry about having enough physicians in this country. Also there is another factor, and that is, there is very little chance that they are going to default on their loans once they begin producing income. But they are in danger of going into forbearance before they start earning more money under the new system.

I would very much—if you have an answer for that now, fine. Otherwise, I would very much appreciate you looking at this, seeing what can be done to basically restore something close to the 20/220 pathway.

Secretary SPELLINGS. My understanding, as I said, Congressman, is that we have retained that as a transition to the new system that you all enacted as part of the CCRA. Now, whether there are specific, you know, anecdotal and individual cases, you know, we will have to just look into those.

Mr. EHLERS. I think they are more than anecdotal and small numbers. I would appreciate you checking into that, and will be happy to work with you in that.

Thank you. Yield back.

Chairman MILLER. Thank you, Madam Secretary.

Mr. McKeon, did you have a question?

Okay.

Thank you very much for your appearance and for the information that you have imparted to us.

I think you can tell from the questions and sometimes the sense of urgency in my colleagues' voices, this is a problem—as one of them said, they are not looking forward to having hundreds of people calling their office if there is a breach in the system.

Secretary SPELLINGS. Nor am I.

Chairman MILLER. And I think it really is a question of whether or not, having been warned and having seen serious problems in other parts of the credit markets, the question is whether or not we will be able to put together that seamless system for those families and for those students.

And, you know, when I was in the Merchant Marines a number of years ago, first they would brief you on what a lifeboat drill was, and then you would have the lifeboat drill, and then eventually you would have to get in the lifeboats to make sure that everything worked, that the pulleys worked, that the winches worked, and everything would work, and that you could launch the lifeboats. Never had to use them, but we ran through it several times.

And when I was in the Department of Forestry, you constantly had fire drills. And you had to show that you could hook up all of the hoses, that you could put water onto a fire, whether it was residential or whether it was a forest fire. Never had to use the residential, but we knew how to do it.

When I was in the refinery, we constantly had preparation for explosions, for accidents. Fortunately, when I was there, never had to use them, but we were constantly prepared, and we had constant walk-throughs to make sure that everybody knew exactly what they were going to do.

You know, the great heavyweight champion of the world, Rocky Marciano, once said that everybody has a plan right up until the time they get hit. And we find out, more often than not, in Government, that is the case when the incident comes along.

And I think this hearing really is about whether or not we have the confidence—if we can handle the worst, we can handle the best. What we are really talking about here, as I keep saying, is making operational a standby plan.

Every member of this committee would prefer that the FFEL program will continue to operate. But we want to make sure that, in the event that we have a serious gap in the availability of loans under the FFEL program, that you will have the ability to make a choice, or the institutions will have the choice, of going to the Lender of Last Resort, as was envisioned under the law, and/or the Direct Loan program.

I consider these standby authorities. And because they are standby authorities, we have the time to put in place the procedures and the operational protocols. I think that means that we have to move from monitoring to sit-down meetings with the impacted parties, the guaranty agencies, to hear their concerns and to work out an agreement, so, again, if necessary, we will be able to take the preparation and make it operational.

I think, again, the schools need to know whether they want—how and how long it will take them to create a standby authority on the Direct Loan program, should they choose to do that.

Apparently it was fairly seamless, or appears for the moment, for Penn State to make this switch. They were in the FFEL program. That program apparently not able to meet their needs, they were able to make the switch seamlessly for those parents and students.

That is the goal of this committee. We need your cooperation. You need the Secretary of Treasury's cooperation. And I think we need some face-to-face discussions between the guaranty agencies

who may have to stand in stead of these other organizations that might find themselves in a position that they can't meet their historical demand for student loans if the credit markets continue in the state of dysfunction that they currently are.

We all hope that that will cease also. And, obviously, the Secretary of the Treasury and the Chairman of the Fed and this Congress are working hard to try to make that reality come to pass, where we go back to both liquid and stable credit markets. But this is only in anticipation.

So thank you for your time.

And I don't know if you want to make a comment, but clearly this is an opportunity to demonstrate that, with some notice, we can properly plan to mitigate the anxiety and maybe the harm to students and families in additional costs to them if plans are not in place.

Thank you.

Secretary SPELLINGS. Yes, Mr. Chairman, thank you for those comments. And I can assure you we are doing those things and will continue to.

Two things strike me today.

One is that this is highly organic. We are learning, as you are, every day the various dimensions of this. And I think regularized communications between us, maybe not in this formal of a setting, are certainly in order as we go through what will be the busy season, the high season of this industry.

And I would also say, particularly since I have heard many of you talk about specific institutional stories or anecdotes, please let us know those things, and we will run those to ground and do everything we can to make sure that there is capacity in the system.

Chairman MILLER. Yes.

Mr. Platts? You are now on the Secretary's time, so you do whatever you want. [Laughter.]

Thank you, Madam Secretary.

Mr. PLATTS. Thank you, Mr. Chairman and Madam Secretary, for yielding time to me. So I will be very brief. And I don't want to be repetitive, but I do want to associate myself with Mr. Altmire's comments and questions earlier in Pennsylvania's situation.

And I know you are very familiar—and Senator Specter, Senator Casey and most of us House members have written to you, as well as Secretary Paulson and the Federal Reserve. My understanding thus far, the Fed has responded saying they defer to you and Secretary Paulson on how to address the specific challenge across the country and then specific to us in Pennsylvania.

And so I just want to, I guess, reaffirm Mr. Altmire's emphasis on how critical this is to students, as we know best in Pennsylvania, and that survival and strengthening of the FFEL program to allow PHEAA and other agencies like it to be re-engaged is critical to students getting access to the assistance they need.

And as one who, you know, paid off my last student loans as a Member of Congress from undergrad and law school, I personally understand the importance of these programs and, you know, just look forward to working with you and the Department to make sure that that competition is there and the choice is there and, bot-

tom line, the access is there for the students across the country, and, obviously, especially focused on Pennsylvania.

So thank you, Mr. Chairman.

And, Madam Secretary, thank you.

Secretary SPELLINGS. Thank you, Congressman.

Chairman MILLER. Thank you.

Thank you, Madam Secretary. We will continue to be in touch with you. Thank you.

The next panel to come before the committee will be made up of Mr. Paul Wozniak, who is the managing director of the Education Loan Group of UBS Securities. Mr. Wozniak is the managing director of UBS Educational Loan Group, and is now in his 26th year in the field of education lending. Mr. Wozniak is also involved in all aspects of investment banking, both Federal and private education loans, including assistance on structural economic credit program matters, and an active participant in the education loan community.

Terry Muilenburg is the Senior Vice President of USA Funds, and whose function is to help administer the FFEL program. And in this position, she is responsible for representing USA Funds' interests in the Federal Government and works closely with other student loan organizations in the development of legislative and regulatory agenda.

Roberta Johnson is the Director of the Office of Student Financial Aid at Iowa State University in Ames, Iowa. And prior to assuming that role as director of student aid at Iowa University, Johnson served 18 years as the assistant director and associate director positions at Iowa State, where she was responsible for student loan operations.

Sarah Bauder is the Director of Student Financial Aid at the University of Maryland, College Park, Maryland. And she began her career in financial aid in 1990 as a financial aid counselor at St. Mary's College in Maryland. After 6 years, she accepted the position at the University of Maryland-College Park campus as assistant director for loan processing. She then moved to the position of associate director for operations and assistance, where she managed a $100 million student loan program, scholarships, athletic verification, and quality assurance.

Charles C. Sanders—oh, excuse me, Mr. Wilson, did you want to introduce Mr. Sanders?

Mr. WILSON. Yes, thank you.

Chairman MILLER. Yes, thank you.

I yield to Mr. Wilson.

Mr. WILSON. Thank you, Mr. Chairman.

It is an honor for me to welcome Mr. Chuck Sanders here today. He is a neighbor. He is from my home State of South Carolina and on the panel today.

Mr. SANDERS currently serves as president and CEO of the South Carolina Student Loan Corporation. In that position, he is responsible for the day-to-day management and coordination of all corporate business activities. Prior to this position, Mr. Sanders served as director of investments and debt management for the South Carolina State Treasurer's Office for 13 years.

Mr. SANDERS currently serves on the board of directors of Anderson University, the South Carolina Independent Colleges and Universities, the Greater Columbia Educational Advancement Foundation, the executive board of the South Carolina Association of Student Financial Aid Administrators, and is a board member and vice chairman of the Education Finance Council.

He received his bachelor of science degree in banking from the University of South Carolina.

I know from touring his office last month that he and his very capable and dedicated staff are student-friendly, giving opportunity for the young people of South Carolina. And I welcome Mr. Sanders here today.

And I yield back the balance of my time. Thank you, Mr. Chairman.

Chairman MILLER. Thank you.

Mr. Wozniak, we are going to begin with you.

There will be a light. A green light will go on when you begin to testify—you are familiar with this—and then an orange light when you have a minute left, at which point we hope you will be able to wrap up your remarks. But, again, we want you to complete your thoughts. And then a red light.

Let me say this to the panel. To the extent you feel a need to comment on something that you heard in the exchanges that took place in the previous panel with the Secretary, please feel free to do so. That would be helpful to us.

Your entire statements will be placed in the record in their written form, and so you proceed in the manner in which you are most comfortable.

Mr. Wozniak, welcome. Thank you.

**STATEMENT OF PAUL WOZNIAK, MANAGING DIRECTOR AND MANAGER, EDUCATION LOAN GROUP, UBS SECURITIES, LLC**

Mr. WOZNIAK. Chairman Miller, Ranking Member McKeon, members of the committee, thank you very much for inviting me today.

I am Paul Wozniak, managing director and group manager of the UBS Securities, LLC. The group is one of the largest of its kind on Wall Street, and we are mandated to coordinate all education-related financing activity in the fixed-income department, which includes both asset-backed finance as well as municipal securities.

I am currently in my 26th year of financing postsecondary loans, following my borrowing under the FFEL program as well.

$54 billion of Stafford and PLUS FFELP loans were originated in 2007-2008 academic year, primarily by banks, private and public nonbank corporations, State agencies, and not-for-profit corporations. If patterns held as in past years, because the information is the latest available, banks probably accounted for about 60 percent of loan originations.

However, when one observes the holders of loans, after the fact in the long-term markets, the market share of outstanding loans falls to less than 24 percent. And this is important in trying to understand how ultimately the student loan program is financed. Just like Fannie Mae and Freddie Mac provide secondary market support to the mortgage market, that is, in many regards, what many

of the corporations and not-for-profit operations do for the student loan marketplace.

Banks, as deposit-taking institutions, have a general cost advantage to entities that are required to access the capital markets through securitizations or other means. They must also allocate costs of capital and reserves, but, on the margin, they should maintain a funding advantage over those raising money in the capital markets.

Further, for those banks who originate and sell their loans to other holders in the secondary market—and that appears to be the majority of the 2,000-some banks in the program—funding needs are both modest in size and short-term in nature.

The remaining participants in the FFELP program, those who are holders of more than three-quarters of all FFELP loans outstanding, rely on the capital markets for their funding source. This generally takes several forms. Most of these entities use some type of warehousing program initially—commercial paper, a line of credit—and then those are usually less-than-364-day facilities. They do that to accumulate enough assets to have an efficient financing program that will meet both rating agency and investor acceptance. These facilities generally must be cleaned out once a year.

As Secretary Paulson said yesterday, the securitization of student loans actually has led to greater availability and lower costs. And, in fact, the most common form of refinancing or take-out is securitization.

And this has taken the form of floating rate notes. Securitization is merely the creation of a trust which issues securities to investors. The trust uses the proceeds to acquire a pool of loans, usually from a warehouse facility, and that line of credit is paid down.

The trust is structured to allow investors to solely look at the underlying loan collateral for repayment of the investment. And this is important, because it insulates the investor from any negative credit event that may befall the sponsor of the trust. As a result, the trust receives a higher rating than it could if corporate-issuer risk were also a continued possibility. And, therefore, it offers a lower rate of return to the investor, given those protections. Alternatively, the trust is required to perform on its own with no additional support from the lender.

It should be known also that banks also make themselves available to the Floating Rate Note securitization market. Indeed, while banks are holders of less than one-quarter of all FFELP loans, banks who also securitize include about three-quarters of those institutions, of those deposit-making institutions. So, said another way, you might assume that about only 10 percent of the loans outstanding are funded by deposits.

Another option has been the auction rate market. The FRN market has been growing much faster than the auction rate market. The auction rate market is about one-third the size of the FRN market outstanding.

Auctions certainly have been in the headlines recently. And as issuers have looked out over their funding options, given the low margins available on the loan product, they weighed the advantages of using an FRN versus the advantages of an auction structure. Auctions permit a high degree of financing efficiency, and

they act in combination as a warehouse facility, term financing at a reasonable and variable rate cost of funds. Their ability to be redeemed and converted to other structures is also a very positive feature.

For 15 years they performed exceptionally well. There were 150,000 auctions, I would estimate, without a single failure. Recently, however, that has ended. That has created additional problems. And I will just say that the cost of financing has risen both on the FRN side and the auction rate by approximately 100 basis points. The burden on this marketplace is significant and real, and it is unlikely to be able to correct itself and avoid having an impact on access to loans.

[The statement of Mr. Wozniak follows:]

**Prepared Statement of Paul W. Wozniak, Managing Director, UBS Securities LLC**

Good Morning. I am Paul Wozniak, a Managing Director and Group Manager of UBS Securities LLC. The group is one of the largest of its kind on Wall Street, and we are mandated to coordinate all education loan related finance activities in the Fixed Income department, which includes asset-backed finance and municipal securities. I am currently in my 26th year of financing postsecondary education loans.

$54 billion of Stafford and PLUS FFELP loans were originated in the 2007-2008 academic year, primarily by banks, private and public non-bank corporations, state agencies and not-for- profit corporations. If patterns held as in years past, banks probably accounted for approximately 60% of loan originations—as they did in the prior year which is the last year for which data were available. However, when one observes holders of loans, banks' market share of outstanding loans falls to less than 24%. This is important when trying to understand how entities finance themselves.

Banks, as deposit taking institutions have a general cost advantage to entities that are required to access the capital markets through securitizations or other means. They must also allocate costs of capital and reserves, but on the margin, they should maintain a funding advantage over those raising money in the capital markets. Further, for those banks that originate and sell their loans to other holders in the secondary market, which appears to be the majority of banks, their funding needs are both modest in size and short-term in nature.

The remaining participants in the FFELP program, those who are holders of more than three-quarters of all FFELP loans outstanding, rely on the capital markets for their funding source. This generally takes several forms. Most of these entities will use some type of warehousing program or line of credit—a commercial paper conduit or bank loan—with terms that are generally renegotiated every 364-days and permit the FFELP lender to accumulate a sufficient amount of loans to accomplish an efficient financing program that will meet rating agency and investor acceptance. These credit lines must generally be cleaned out into some other financing program at least once per year.

The most common form of refinancing or 'take-out' is a securitization. Primarily this has taken the form of the issuance of Floating Rate Notes or FRN's. A securitization is merely the creation of a trust which issues securities to investors. The trust uses the proceeds to acquire a pool of loans from the warehouse facility, and the warehouse line of credit is paid down. The securitization trust is structured to allow the investor to solely look to the underlying loan collateral for repayment of the investment. This is important because this insulates the investor from any negative credit event that may befall the sponsor of the trust. As a result, the trust receives a higher rating than it would if corporate issuer risk continued as a possibility, and therefore the FRN's bear a lower interest rate spread than it would if it were not so insulated. Alternatively, the trust is required to perform on its own with no additional support from the lender.

It should also be noted that banks also avail themselves of the Floating Rate Note securitization market. Indeed, while banks are holders of less than one-quarter of all outstanding FFELP loans, banks accounting for about 75% of these holdings use or are prepared to use FRN securitizations to finance their portfolios to some extent. Banks do this because it diversifies the funding sources of their assets. While it may be a more expensive cost of funds than deposits, the diversification of funds and the potential for off-balance sheet funding requires its consideration.

Another option that has been used extensively, and more so among state agencies and not-for-profit corporations, has been the auction rate securities market. The education loan backed auction market is now only about ⅓ of the size of the education loan FRN securitization market. In recent years, issuance of FRNs has greatly exceeded the issuance of taxable auction rate securities, especially to finance pre-10/1/2007 originated consolidation loans during the heavy origination era of those loans. Issuers had to weigh the advantages of a fixed spread FRN against the advantages of the auction structure. Auctions permitted a high degree of financing efficiency, in that they acted as a combination warehouse facility and term financing at a reasonable and variable rate cost of funds. Their ability to be redeemed or converted to other structures without significant cost was also a very positive feature. Given the relatively narrow spread on FFELP student loans, it is important to have a highly efficient, flexible financing vehicle.

For 15 years the auction product performed exceptionally well. It was able to withstand numerous market shocks such as the 1994 bond market which at the time was described as the worst since the great depression, the 1998 Russian debt crises, Y2K and an accounting reclassification event in 2004. These tests of the product seemed to show its resilience. Interest rate spreads would widen, and then return to previous levels. For, what I would estimate as 150,000 auctions of education loan backed collateral; the market had never experienced a failed auction (where auction sales exceeded purchases and holds). That ended recently. As a consequence, the ensuing days resulted in significant auction sales resulting in a complete and total failure of the auction market. This was compounded by the problems facing the monoline insurance companies, encouraging sales and reducing restructuring options.

As a result of the continuing liquidity crisis, the deleveraging of investor balance sheets and the failure of the education loan backed auction market, the cost of funds to holders of loans has risen significantly. Those with auction rate securities are incurring a penalty interest rate. Those with warehouse facilities, to the extent that renewals are available, are incurring a much higher rate as well as the requirement of posting significantly more equity than had previously been required. There are approximately $150 billion of education loans currently financed via these two methods. For those who would refinance these loans into a fixed spread FRN structure, they face (i) interest rate spreads that may be a full 1% (100 basis points) higher, (ii) the inability to currently finance certain loans with long average lives (consolidation loans) due to lack of investor demand, and (iii) the need to add significant and costly equity into a structure based on new rating agency assumptions borne of the current market environment. The burden on this marketplace is significant and real and is unlikely to correct itself to avoid having an impact on access to loans.

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Chairman MILLER. Thank you.

## STATEMENT OF TERRY MUILENBURG, SENIOR VICE PRESIDENT, USA FUNDS

Ms. MUILENBURG. Chairman Miller, Ranking Member McKeon, members of the Committee, all of us here today share a strong commitment to ensuring that every eligible student——

Chairman MILLER. I would ask you to pull the microphone a little bit closer to you.

Ms. MUILENBURG. All of us here today share a strong commitment to ensuring that every eligible student seeking Federal Family Education Loans will have an uninterrupted source of loan capital to pursue higher education. I am here on behalf of United Student Aid Funds, a 48-year-old nonprofit organization that works to enhance higher education preparedness, access and success. Last year we guaranteed $25.8 billion in FFEL loans, or about one-fourth of all such loans issued.

USA Funds and the other 34 guarantors, all of whom are either State agencies or nonprofit organizations, perform a critical role in the delivery of student aid. Together we administer every loan made under the FFEL program with an outstanding portfolio of over $400 billion. Through our efforts we protect the Federal in-

vestment in our students through delinquency prevention, default diversion and debt management programs.

Consistent with guarantor's public purpose mission, we provide an extensive range of services and programs to increase awareness of the importance of higher education, the opportunities available and the financial support offered. We believe the more borrowers know about personal finance and borrowing wisely, the better prepared and more likely they are to successfully meet their financial obligations.

We strongly emphasize the need for students to exhaust all eligibility for free money and grants and scholarships before turning to Federal loans, and advise against turning to more expensive private loans unless absolutely necessary, and then only to cover essential educational costs.

Guarantors primary focus is default prevention. We begin this effort through financial literacy programs that begin early on and include intensive counseling on the options available to avoid default if the borrower falls behind on their loan payments. Thanks in part to these comprehensive efforts, the most recent national student loan default rate is 4.6 percent, one of the lowest rates in the history of the program.

Turning to the topic of this hearing, we first of all very much appreciate the remarks of members of the committee to the Secretary and Larry Warder with respect to the need for a school-based certification program, the need to ensure that we can use electronic processes on these loans, that we are able to sell these loans and that it would be very important for us to be able to sit down with the Department prior to their issuing guidance with respect to implementation of an LLR program.

We first and foremost urge the administration, with support from Congress, to examine and pursue all available alternatives to address the liquidity issues in the credit markets as the preferred means of addressing the challenges many educational lenders are currently facing.

At the same time, guarantors are required under the Higher Education Act to arrange for or serve as a Lender of Last Resort. The LLR program is just that, a safety net to assure uninterrupted access to needed loan funds. The act has provided this authority for decades, but LLR loans have been used in only limited circumstances. Using nonFederal monies, these narrowly focused programs were not intended to address broad-scale disruption in the lending market. They have largely relied on the capacity of lenders to make loans which carry 100 percent insurance in order to encourage lenders to participate.

In the event of a more serious or widespread loan access problem, the Higher Education Act authorizes the Secretary of Education to advance funds to guarantors to make LLR loans. As we have discussed earlier, the Department last considered using this authority in 1998. The Department at that time asked three guarantors, including USA Funds, to be prepared to administer LLR programs using Federal advances, based on an agreement developed by the guarantors and the Department. It is my understanding that these same arrangements would have been offered to

the other guarantors desiring to participate and willing to abide by the same terms and conditions.

Of course these agreements were never implemented due to congressional action to modify the interest rate formula and ensure continued FFEL participation by lenders well before any problems would have developed. Those agreements provided for the Department to make advances, for guarantors to make LLR loans, a determination by the Secretary as to where each guaranty agency could issue such loans, and a school-based rather than a borrower-based process so that borrowers would not individually have to prove that they had been turned down by two lenders.

Given the current situation with the credit markets it is essential that all parties be prepared to step in quickly and effectively so that every eligible student has access to Federal student loan funds. For this reason USA Funds urges the Department to sit down promptly with guarantors and develop specific plans that could be quickly implemented should it become necessary to activate an LLR program using Federal advances.

I offer a few suggestions regarding how the Department might proceed. First, again as we have discussed, it should be a school-based rather than a borrower-based process. Clearly the Department in 1998 felt that it had the legal authority to implement a school-based rather than a borrower-based program. And I don't see why that should be any different today than it was then. The Department, upon the request of the school, should determine whether students attending that school are able to secure loans. The school should check with its existing lenders before making such a request. A school-based certification would both simplify and expedite it. From the borrower perspective it would be the same as it is today, consistent with the school's application process, with no additional hoops.

Mr. Chairman, the bottom line is we hope the phone won't ring at 3:00 a.m. but if it does, we will answer the call. Thank you very much.

[The statement of Ms. Muilenburg follows:]

**Prepared Statement of Terry L. Muilenburg, Senior Vice President, Government and Industry Relations, United Student Aid Funds, Inc.**

Chairman Miller, Ranking Member McKeon, Members of the Committee, I am pleased to have the opportunity to testify this morning. All of us here today share a strong commitment to ensuring that every eligible student seeking federal student loans will have an uninterrupted source of loan capital to pursue postsecondary education.

I am here today on behalf of United Student Aid Funds, a 48-year old nonprofit organization that works to enhance postsecondary-education preparedness, access and success. Last year, USA Funds guaranteed $25.8 billion in Stafford, PLUS and Consolidation loans, or about one-fourth of all Federal Family Education Loans issued in fiscal year 2007.

USA Funds and the other 34 guarantors, all of whom are either state agencies or nonprofit organizations, perform a critical role in the delivery of student financial aid. Together, we administer every student loan made under the Federal Family Education Loan Program, with an outstanding loan portfolio of over $400 billion. Through our efforts, we protect the Federal Government's investment in our students through delinquency prevention, default aversion and debt management programs. We also work with students, families, colleges, universities, career schools, secondary schools and higher education finance colleagues to provide information on educational opportunities and financial literacy programs that help students realize their higher education dreams.

As you will note in this testimony, guarantors are involved with students over the long term: Our work with students begins as early as elementary school, through early awareness and outreach programs, and does not end until they have repaid their loans. Many guarantors, including USA Funds, provide early awareness, financial literacy and debt management materials in Spanish, as well as English, to ensure that Hispanic students and families, the fastest growing demographic segment of the population, are able to fully benefit from these services.

Guarantors are also committed to accountability. In addition to serving students, families and schools, we are resolute in fulfilling our responsibilities to the Congress, the Department of Education and the American taxpayer.

*Promoting College Access*

Consistent with our public service mission, guarantors provide an extensive range of services and programs to increase awareness of the importance of higher education, the opportunities available and the financial support offered. The College Access Initiative, established by the Deficit Reduction Act of 2005, formalized a fundamental role for student loan guarantors in promoting access to postsecondary education. We appreciate your recognition of this work by codifying our responsibility to do so.

Through our college access efforts, guarantors are filling a local need that often cannot be met by the secondary school counselor. According to a survey by the National Association for College Admission Counseling, the national student-to-counselor ratio for public high schools is 315-to-1. Thus, despite diligent efforts on the part of school personnel, too many students still struggle to understand their options for postsecondary education and how to obtain financial aid. Throughout the country, guarantors step in to help prevent students from falling through the cracks. For example, last year guarantors:

- Distributed millions of college awareness, financial aid and financial literacy brochures, guides and toolkits to schools, students and families. USA Funds alone distributed over 4 million publications to help families plan and pay for college. These materials provide in-depth information on: saving and paying for college, planning for a career, money management, applying for financial aid, and available scholarships and grants.
- Organized and participated in more than 8,400 financial aid workshops and events that reached more than 900,000 students and families and more than 7,800 school guidance counselors. These workshops provide hands-on training for completing the Free Application for Federal Student Aid, and understanding the types of financial aid available, as well as the college application process.

*Improving Financial Literacy and Preserving Low Default Rates*

Guarantors focus significant efforts on improving the financial literacy of students and families. For example, USA Funds' financial literacy program, Life Skills, is in use at over 500 postsecondary institutions nationwide. We believe that the more borrowers know about personal finance, money management, and borrowing wisely, the better prepared and more likely they are to meet their financial obligations. To accomplish that goal, guarantors provide detailed financial literacy materials, training sessions and interactive tools to assist all students and schools in understanding prudent borrowing and repayment and successful money management. Guarantors, including USA Funds, emphasize the need for students to exhaust all eligibility for "free" money in grants and scholarships before turning to federal loans, and advise against turning to more expensive private loans unless absolutely necessary, and then only to cover essential educational costs. Below are examples of financial literacy activities:

- Developing Web sites and distributing materials designed for students and families to understand how to handle their finances as they prepare for college and beyond
- Working with local education centers to implement early financial literacy programs with area high schools
- Developing financial-literacy materials for graduate and professional students and adult learners to teach students about time- and money-management practices that will permit them to graduate on time, with minimal education debt, and prepared to repay the student loans that financed their education.

In addition to improving financial literacy, intensive efforts are involved in counseling borrowers on their repayment obligations and options to prevent defaults. These efforts include:

- Creating comprehensive, state-of-the-art default aversion programs, including tools schools can use to contact their former students;

• Counseling the delinquent borrower on the consequences of default and the options available to avoid default; and

• Assisting the borrower in obtaining the most reasonable repayment terms possible, a deferment, or a forbearance.

In USA Funds' case, we successfully resolve more than nine out of ten past-due accounts, and as a result, last year we prevented $16.7 billion in potential loan defaults.

Thanks in part to these comprehensive efforts, the national student loan default rate is 4.6 percent, one of the lowest rates in the history of the program, with USA Funds below the national average at 4.0 percent. I would like to thank the Committee for specifically recognizing these financial literacy, delinquency and default prevention activities as essential roles for guarantors in the College Opportunity and Affordability Act (H.R. 4137) and encourage you to include these provisions in the final conference agreement on the Higher Education Act reauthorization bill.

*Lender of Last Resort Programs*

Turning to the topic of today's hearing, guarantors are statutorily required under the Higher Education Act to serve as, or arrange for, a backstop Lender of Last Resort (LLR) to address situations where eligible students and parents are unable to obtain Federal Family Education Loans. The statute requires guarantors to provide, or arrange with an eligible lender to provide, LLR loans in each state where it serves as the designated guarantor. Guarantors are required to have policies and operating procedures in place to address LLR situations. USA Funds has such procedures and, to my knowledge, so do all other guarantors.

Lenders of last resort programs are just that: a safety net to assure uninterrupted access to needed loan funds. The Act has provided this authority for decades, but lender of last resort loans have been made in only limited situations. Using non-federal monies, these narrowly-focused programs were not intended to address broad scale disruption in the lending market. They have largely relied on the capacity of lenders to step up and make loans, which carry 100 percent insurance to encourage lenders to participate.

In the event of a more serious or widespread loan access problem, the Higher Education Act authorizes the Secretary of Education to advance funds to guarantors to make LLR loans. The availability of federal capital assures that loan funds will be available. The Department last considered using this authority in 1998 when, due to an impending change in the interest rate formula, there was concern that lenders might not make loans. The Department then asked three guarantors, USA Funds, Great Lakes Higher Education Corporation, and the Pennsylvania Higher Education Assistance Agency, to be prepared to administer lender of last resort programs using federal funds, based on an agreement developed by the guarantors and the Department. It is my understanding that the same arrangements would have been offered to other guarantors desiring to participate and willing to abide by the terms and conditions included in these agreements.

These agreements, which were never implemented due to Congressional action to modify the interest rate formula and ensure continued FFELP participation by lenders—well before a crisis could have occurred—provided for:

• Authority for the Department to make advances to guarantors for the purpose of making LLR loans;

• A determination by the Secretary as to where each guarantor could issue LLR loans;

• A school-based, rather than a borrower-based LLR process so that borrowers would not individually have to prove that they were turned down by two lenders;

• Insurance on LLR loans at 100 percent;

• Fees to guarantors making LLR loans with federal advances, intended to cover the costs of issuing and maintaining the loans, in lieu of the special allowance payments normally paid to lenders;

• Guarantor repayment of advances upon request of the Department, with the Department able to require assignment of LLR loans to the Secretary, and upon assignment, the portion of any advances represented by the loans would be considered repaid; and

• Eligibility for interest benefits and special allowance payments for a purchasing lender in the event an LLR loan was sold.

The Lender of Last Resort provisions in the HEA are truly a last resort to ensure student access to loans for higher education. Given the current situation with the credit markets, it is essential that all parties be prepared to step in to address a situation where students are unable to obtain federal student loans. It is critical that all stakeholders are prepared to act quickly and effectively, so that every student at every Title IV eligible institution has access to Federal student loan funds.

For this reason, USA Funds strongly encourages the Department to promptly work with guarantors to develop specific plans that could be quickly implemented should it become necessary to activate an LLR program.

I offer a few suggestions regarding how the Department might proceed as it considers the need for lenders of last resort.

- First, USA Funds and our guarantor colleagues believe eligibility for lender of last resort loans should be school-based, rather than borrower-based. That is, the Department, upon request from a school, should determine whether students attending the school are able to secure loans. The school should check with its existing lenders before making such a request. Once the Department is satisfied as to the need for last resort lending, all students at the school should be eligible for the program. Students should not have to qualify individually. A school-based determination of eligibility would both simplify and expedite the process. From a borrower perspective, the application process would be the same as it normally would be, consistent with the school's loan application process flow. When the loan reaches USA Funds for guarantee, the loan would be "flagged" in our guarantee and servicing system as an LLR loan and tracked throughout its lifecycle as such.
- Second, I would also recommend that the Department work with guarantors to ensure that the operational processes involved in funding and making LLR loans reflect an electronic loan processing environment.
- Third, as in the 1998 agreements, guarantors should be permitted to sell LLR loans made with federal advances, with the proceeds used to repay such advances.

At the same time, we urge the Administration, with support from Congress, to examine all available alternatives to address the liquidity issues in the credit markets as a preferred means of addressing the challenges many education lenders are currently facing.

These are challenging times in the student loan marketplace, but with foresight and prudent planning, we can ensure uninterrupted access to student loans. We stand ready to work with the Department, Congress, lenders and our school colleagues to ensure that every eligible student and parent receives the federal student loans to which they are entitled.

Thank you.

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Chairman MILLER. Ms. Johnson.

## STATEMENT OF ROBERTA JOHNSON, DIRECTOR OF STUDENT FINANCIAL AID, IOWA STATE UNIVERSITY

Ms. JOHNSON. Thank you, Mr. Chairman and members of the committee. I am from Iowa State University located in Ames, Iowa, and proudly celebrating our 150th anniversary this year. Iowa State University is a land grant institution with an enrollment of 26,160 students. Prior to assuming the role of Director of Student Financial Aid, I served for 18 years in the Assistant Director and Associate Director positions at Iowa State where I was responsible for student loan operations. I have experience in the administration of loans through both the Federal Family Education Loan program and the Federal Direct Loan program.

Iowa State University did enter the Federal Direct Loan program as a year-one school in 1994. Iowa State University's loan volume in the Federal Direct, Stafford, and PLUS loan for 2006-2007 was $97.6 million. It encompassed over 20,000 separate awards for 14,645 students. Yet we were able to accomplish this with only two full-time staff members. One of those staff members also administers the Federal Pell Grant program, Academic Competitiveness Grant, National SMART Grant, and will assume duties for the TEACH Grant program in July when that program becomes operational.

There were a number of reasons why we moved to Direct lending in 1994 and why we remain there today. Most notably, we are able to provide better customer services to our students and their par-

ents, minimize the amount of staff time spent dealing tracking down loan funds or changes, and maximize the predictability of receiving funds both for our students and our institution.

Our students and their parents frequently comment on how easy it is to understand the process; that they appreciate always knowing who holds their loan; and that Iowa State University provides prompt, courteous service when they have questions about any financial aid program. Before direct lending at my institution, that was not the case.

In my further testimony that I have provided, which I am not going to comment on directly, I have included some slides, including one which is a GAO slide which quite accurately depicts what Iowa State University experienced as a participant in the FFEL program dealing with multiple student loan players and the contrasting graphic that shows how the process works today in the Direct Loan program.

The Direct Loan program has been described as Pell with a prom note. In fact any school, FFEL or DL, that is currently administering the Federal Pell Grant, ACG or National SMART Grant programs is already interfacing with the Department of Education's system for disbursing direct loans and other student aid. This system is called the common origination and disbursement system.

To participate in the Direct Loan program, as has been mentioned earlier, requires only that a school sign up to participate with the Department of Education and that they then just add loan information to the files that they are already sending to the Department via this common origination and disbursement system.

In the midst of the current credit crunch and with daily media reports about student loan instability, I think it is very important that we help students and their families differentiate between Federal and private loans and to reassure them that Stafford loans, PLUS loans, and Grad PLUS loans are available.

While we have heard that there have been reports of certain FFEL lenders leaving the program, temporarily suspending operations, or redlining certain schools due to graduation or default rates, this is not the case in the Federal Direct Loan program. The Direct Loans are funded as a student entitlement from funds borrowed wholesale from the private sector through the sale of Treasury securities, and there is never a question of capital availability in the Direct Loan program. This is different than FFEL in that in that program the lenders are entitled to subsidy and default payments if they choose to make loans to students.

The Direct Loan program also is administered by private sector contractors through competitively led contracts by the Department of Education. These contractors have years of experience administering Direct Loans, and indeed many of them are also services for the FFEL lenders. Like the FFEL program the Department's responsibilities are to oversee and govern the administration of both programs.

In 1994 the Direct Loan program was entirely new. In 3 years it had one-third of the market and the program worked smoothly. Today it has 20 percent of the market, thanks to marketing and taxpayer-provided discounts that were offered to schools to induce

them into the FFEL program and the prohibition against marketing of Direct Loans by the Department.

The Department of Education already does have the infrastructure to handle an influx of schools into the Direct Loan program, as we heard Secretary Spellings indicate earlier.

Mr. Chairman, I thank you for the opportunity to appear before you today and for your support and the support of others on the committee for direct lending.

I would be happy to respond to any questions that you might have later.

Chairman MILLER. Thank you very much.

[The statement of Ms. Johnson follows:]

**Prepared Statement of Roberta Johnson, Director of Financial Aid, Iowa State University**

Mr. Chairman and Members of the Committee: My name is Roberta Johnson and I am the Director of Student Financial Aid at Iowa State University in Ames, Iowa. Iowa State University is a land-grant institution with an enrollment of 26,160. Prior to assuming the role of Director of Student Financial Aid at Iowa State University, I served for eighteen years in the assistant director and associate director positions at Iowa State where I was responsible for student loan operations. I have experience in the administration of loans through both the Federal Family Education Loan Program and the Federal Direct Loan Program. Iowa State University entered the Federal Direct Loan Program as a Year One school in 1994.

Iowa State University's loan Federal Direct Stafford and PLUS volume in 2006-07 was $97.6 million dollars and encompassed over 20,000 separate awards for 14,645 students. Yet we were able to accomplish this with only 2 full-time staff members. One of those staff members also administers the Federal Pell Grant program, Academic Competitiveness Grant, National SMART Grant, and will assume duties for the TEACH Grant program in July.

There were a number of reasons why we moved to Direct Lending in 1994 and why we remain there today—most notably, we are able to provide better customer service to our students and their parents; minimize the amount of staff time spent dealing with tracking down loan funds or changes; and maximize the predictability of receiving funds both for our students and our institution. Our students and their parents frequently comment on how easy it is to understand the process, that they appreciate always knowing who holds their loan, and that Iowa State University provides prompt courteous service when they have questions about any financial aid program. Before Direct Lending, that was not the case.

I have included in the attached slides a GAO slide that quite accurately depicts what Iowa State University experienced as a participant in the FFEL program, dealing with multiple student loan players and the contrasting graphic showing how the process works today. The Direct Loan Program has been described as Pell with a Prom Note. In fact, any school that is currently administering the Federal Pell Grant, ACG, or National SMART Grant programs is already interfacing the with Department of Education's system for disbursing Direct Loans and other student aid, the Common Origination and Disbursement (COD) system. To participate in the Direct Loan program would require only that they sign up to participate with the Department of Education and that they attach loan information to the files they are already sending to the Department via COD.

In the midst of the current credit crunch and with daily media reports about student loan instability, it is important to help students and their families differentiate between federal and private loans and to reassure them that Stafford Loans, PLUS loans and Grad PLUS loans are available. While there have been reports of certain FFEL lenders leaving the program, temporarily suspending operations, or redlining certain schools due to graduation or default rates, this is not the case in the Federal Direct Loan Program. Direct Loans are funded as a student entitlement from funds borrowed wholesale from the private sector through the sale of Treasury Securities. There is never a question of capital availability in the Direct Loan Program. This differs from FFEL. In that program lenders are entitled to subsidy and default payments if they choose to make loans to students.

The Direct Loan Program is administered by private sector contractors through competitively let contracts by the Department of Education. These contractors have years of experience administering Direct Loans, and indeed many of them also are

servicers for FFLEP lenders. Like the FFEL program, the Department's responsibilities are to oversee and govern the administration of both programs.

In 1994, the Direct Loan program was entirely new. In three years it had one third of the market and the program worked smoothly. Today it has 20% of the market thanks to the marketing and taxpayer provided discounts FFEL participants offered and the prohibition against marketing of Direct Loans by the Department. The Department of Education already has the infrastructure to handle an influx of schools into the Direct Loan program.

Mr. Chairman, thank you for the opportunity to appear before you today and for your support, and the support of others on the committee, for Direct Lending. I would be happy to respond to any questions you or the Members of the Committee might have.

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Chairman MILLER. Ms. Bauder.

**STATEMENT OF SARAH BAUDER, DIRECTOR OF STUDENT FINANCIAL AID, UNIVERSITY OF MARYLAND**

Ms. BAUDER. Good morning and thank you for having me here. Is this on?

Chairman MILLER. You are on.

Ms. BAUDER. Good. I would like to take a quick moment first and say thank you on behalf of all the 6,000 financial aid administrators out there for increasing the Pell Grant. That $400 difference really does pay for books for a high need student in Pell Grants. We really have been fighting to get that increase, so thank you to have the opportunity to do that.

I am the Director of Student Financial Aid at the University of Maryland, just a hop, skip, and jump up the road here. We have about 35,000 students on campus. And let me break that down for you. We have about 75 percent of those students file the FAFSA form. Of those students who file the FAFSA form, about 90 percent accept their student loan.

We have about $120 million loan volume. And let me break that down further, because loans are a key component to how we package financial aid. So about $85 million is the Stafford loan, and those are broken out pretty equally between subsidized and unsubsidized loans. We have about $30 million in the Federal PLUS loans for dependent students, and then about $20 million for the Grad PLUS; and then the other $20 million is private loans, bridging that gap between the cost of education, what we have awarded and what the student can afford to pay.

So, student loans, I give you those statistics to show that student loans truly are a large component of what we do in financial aid.

The timing of this hearing actually couldn't be better. For the last 3 weeks, and nationally this is happening, we have been simulating our packaging, trying to figure out how we are going to spend our money for the upcoming freshman class. And so what we do is we create algorithms and we put all of our pots of money together and we say, okay, here is what we are going to do.

My job as director is to retain and graduate our students. Admissions brings in the students. And we have a little bit of recruitment responsibility in terms of how we package our aid. But the bulk of the responsibility is to make sure we retain and graduate. And so that is a large responsibility on any director.

And so what we are doing, and so as we are simulating here, here are some events. And I want to give you these events because

each one is a brick in and of its own. And we are building a brick wall against inclusion or accessing to education. In and of themselves they are probably inconsequential and we can work around them. But as you build them together, it creates a wall.

The first one we noticed is that consolidation loans are down. Very simplistically, from a director's perspective, is that is a result of having a fixed loan interest rate, not as attractive to students. And then also it is not as attractive to lenders to actually provide that loan because of the cuts in subsidies. That, in and of itself, again is not problematic except that since students aren't consolidating our Perkins loan revolving fund, the loans aren't coming back in to repay that. And so where historically for the last 5 or 6 years we have had approximately between $2.5 million and $3 million to reimburse in new Perkins loan funding, we have less than $200,000. So pretty much it is off the books for Perkins for our upcoming class. That is one brick.

Another one we have is the Work Study and SEOG funds were cut nationally $20 million. That is kind of nickel and dime. And that results in about a $200,000 reduction in those funds for us. Again, very minimal, but when you add it, it becomes problematic.

The third one then is—you know, I read the Wall Street Journal every day and headline news are the subprime mortgage crunch that we are experiencing. And so you couple that then with the cuts in subsidies to lenders and they are scrambling. They are trying to figure out how it is they are going to pay their portfolio.

I am blessed. I am at an institution where lenders want to lend to my students. And I really, truly appreciate the FFEL process and how it has made our institution attractive in terms of its default rate. And I say that because not all institutions have that benefit. We work well with FFEL.

The concerns that I have—and there are two indices in behavior that we are tracking right now that go along with these bricks. And the two of them are the number of appeals that we have from parents and students. And so if we put just for a second our hat on as a parent and say, okay, I am now caught in this subprime mortgage crisis, I am not sure how I am going to pay my mortgage, or I may be facing foreclosure. So here I have that, and yet Johnny and Susie want to go to college. I know my credit score is not quite what it should be.

Now, the lenders don't want to lend high-risk loans or even medium-risk loans. And so if my credit is not pristine in high-credit worthiness I am not going get that PLUS loan, or I am not going to get that private loan. So mom and dad now are appealing to our institution.

So typically what would be what I call "noise" in any one behavior is now we are paying attention to it. So our appeal rate is up about 12 percent while our application rate is up 20 percent. If none of this were happening I could justify it. I am paying attention to it. And I don't have enough longitudinal data to sit here and tell you this is a problem in and of that one data element.

The second data element that we are watching is the percentage of denials in loans. And historically we just put loans together for the creditworthy loans and said here is the denial rate. What we are doing now is we are breaking it out, looking at PLUS loans,

private loans and Grad PLUS loans, and what is the percentage. We are starting to see that tilt up. And so that is problematic and it is concerning, because I have to figure out, come August, when those bills are due, and the students are appealing to us, saying I have this delta or I have this gap that needs to be fed—oh, I am overtime, I am sorry, I will hurry up here—how is it that I am going to pay this? Do I get a female handicap because I can talk?

Chairman MILLER. Go ahead.

Ms. BAUDER. Okay. Thank you.

Let me quickly sum up that we are in the FFEL program. I truly appreciate the FFEL program. I don't see it as just a program of getting the check to the student, but more a holistic program. From the moment the master promissory note is signed to the moment the last payment is made, our FFEL lenders and guarantors are watching our students. And so they exit our campus, those lenders are making sure that loan gets repaid. And I have a chart that shows our default rate and how we are coordinating that. Thank you. I am sorry for taking more time.

[The statement of Ms. Bauder follows:]

**Prepared Statement of Sarah Bauder, Director of Student Financial Aid, University of Maryland**

Mr. Chairman and members of the Committee, thank you for providing me the opportunity to meet with you today about such an important topic. First, I would like to applaud the leadership for increasing the Federal Pell grant program to an historic high. As you know, Federal Pell Grants provide access and affordability to our highest need students. These funds are critical to the retention and graduation goals of our students. Thank you so very much.

As a quick background, I began my career in financial aid in 1990 as a student employee, advancing to Associate Director of Loan Processing at St. Mary's College of Maryland. I then accepted a position at the University of Maryland, College Park campus as an Assistant Director for Loan Processing, was promoted to Associate Director for Operations in 1997 and to Director of Student Financial Aid in January 2005.

Three years ago I had the opportunity to speak with you about the federal loan program and am excited to be here today to provide an historic perspective of what has happened over that time span. It is evident that we are in the calm before the financial storm and I am so encouraged that we are here to plan for what may be hard times ahead. Current economic conditions threaten the overall health of the federal student loan programs. Access, affordability and choice are in jeopardy. We need to assure students and parents that loans are still a viable source for payment of educational expenses. We need to maintain the public confidence in the financial aid programs so that access to education is attainable for all students.

The University of Maryland—a mere eight miles away from the Capitol—is home to over 24,000 undergraduate students and 9000 graduate students. Approximately 75% of all students file the Free Application for Federal Student Aid (FAFSA). Of those students, 90% receive a federal loan, for a total annual loan volume of about $90 million. In addition, we have 3400 Federal Pell Grant recipients. We have a very diverse population with almost 45% being non-white. As the Director of Financial Aid, my job is to provide aid packages which assist in the retention and graduation of our student population, with an effort to reduce debt burden. Given the broad range of students who attend our campus, a 'one-size-fits-all' aid package does not advance those goals. Four years ago, we created the Maryland Pathways program as a means to provide a debt free education to our highest need, Maryland resident students. We currently have over 400 students who benefit from this unique program. In 2005, we added to this program by implementing a Pell Pathways program. This is the only program of its kind nationwide. In this program, we provide additional grant funding to students who come from socio-economic disadvantaged backgrounds who did not receive the Pell Grant because the student earned too much money. Last year, we implemented the Senior Debt Cap, which provides a University of Maryland grant instead of loan for those students who borrowed more than $15,900 in need-based federal loans. We were able to implement

these programs without new monies by coordinating funding strategies with the State of Maryland and shifting our packaging algorithms for the awarding of federal and institutional funding. As you can see by the chart below, our loan indebtedness has decreased due to these programs.

LOAN GUARANTEES BY PROGRAM

| Loan Program | Total 2005–06 | Total 2006–07 | Difference |
|---|---|---|---|
| Stafford Subsidized | $45,287,075 | $43,641,028 | ($1,646,047) |
| Stafford Subsidized | $34,670,529 | $33,230,596 | ($1,439,933) |
| PLUS | $28,887,088 | $26,322,797 | ($2,564,291) |

So how does this impact student loans? Over the last year we've witnessed an array of events that has jeopardized the future of student loans and subsequently our ability to meet the needs of our students. Independently, the events probably would have only caused a ripple; however, when coupled together, the sting is felt in all aspects of financial aid. The financial markets are challenged by the sub-prime mortgage crisis, which has caused investors to back away from asset based securities, which are a source of capital for student lenders. Couple this with the cuts in subsidies to lenders by Congress and we have a formula that equates to lenders scrambling to find funding for their student loan portfolios. Consequently, the ability to lend money to students and parents is negatively impacted.

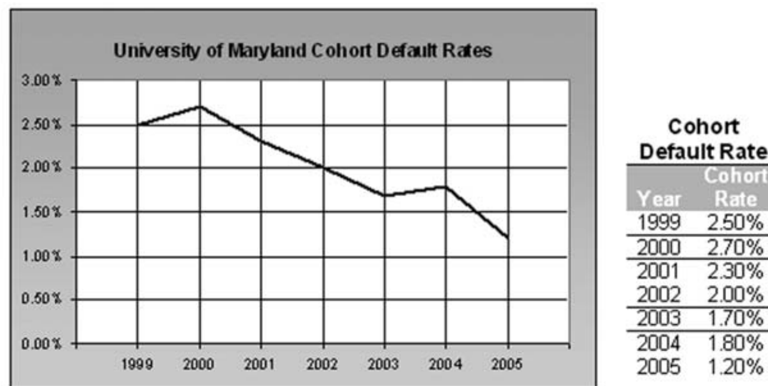
As we enter our peak packaging season, I am concerned about our ability to meet the needs of our students for a variety of reasons. First, consolidation loans which have historically been a financially attractive solution for students have almost disappeared. This in turn has significantly reduced the amount of Perkin's loan repayment. Last year we disbursed $2.3 million in Perkins loan funding. This year (2008-2009), we have less than $200,000 to award to our students. Second, the Federal Work Study Program and the SEOG programs were cut by 20 million dollars nationally. That translates to a $120,000 reduction in SEOG and a $50,000 reduction in Federal Work Study for the University of Maryland. Overall, we have almost 2.5 million dollars less in need based financial assistance to award to our neediest students in the Campus Based Programs. Third, due to the sub-prime mortgage crisis, home equity is less of a resource for families to utilize to pay for the cost of education, as are retirement funds. I have concerns as to the availability of funding options for our families. Couple these events with lenders having to tighten their lending standards, and there are fewer resources available to families to pay for college. Our parents borrow, on average, about $30 million in Federal PLUS loans, while graduate students borrow about $20 million in Graduate PLUS loans. With the overall economic condition, our families and students who typically borrow credit worthy loans will experience increased denial rates.

Since we just completed the packaging of our incoming freshman class, I think it may be helpful to see the impact of these events on an average student. For example, if we superimpose the reduction in aid on a packaging scenario for a typical Maryland resident freshman student, with a zero dollar ($0) expected family contribution (EFC) attending the University of Maryland in academic year 2008-2009, we find that students/families may need to borrow an additional $2770 in loans (see chart below) as compared to the 2007-2008 academic year.

| | 2007–2008 | 2008–2009 |
|---|---|---|
| Direct Cost of Attendance | $17,848 | $18,139 |
| (tuition, fees, room, board, and books) | | |
| Types of Aid: | | |
| Pell Grant | $4,310 | $4,731 |
| SEOG | $1,000 | $500 |
| Federal Work-Study | $2,400 | $1,800 |
| Perkins Loan Funds | $2,000 | $0 |
| Stafford Loan | $3,500 | $3,500 |
| UM Grant Funding | $3,800 | $3,800 |
| TOTAL funding | $17,010 | $14,031 |
| Potential PLUS/Private loan | $838 | $3,608 |

With reduced financing options, families inevitably will need to borrow more funds to pay for college. Further there are fewer lenders providing student loans. One concern circulating among my colleagues is the disruption in the student loan industry as lenders withdraw from the FFEL program. This creates an administrative burden as lender lists need to be revised and students need to be informed to choose another lender. In addition, lender policies are changing. For schools serving high risk students, this may impact their ability to borrow a student loan. As of today, lenders representing 10% of Stafford and PLUS loan origination volume and 30% of consolidation loan volume have either suspended or discontinued their participation in the student loan programs. The University of Maryland never denies choice of lender to a student, which is why we work with over 80 different lenders. As lenders leave the FFEL program, we feel the administrative impact. I am somewhat nervous about the dilemma we are facing in the student loan industry and the availability of funds for our students and the potential disruption this could cause our families.

We review our lender lists every year. As a historical perspective, we've chosen lenders who have quality customer service, advanced technology, excellent pricing, and who advance the mission of our University. Due to the cuts in subsidies, the zero fee loans our students benefited from are disappearing. However, FFEL lenders do advance our mission. One of the missions of our campus is to provide educational services in every aspect of campus, not just in the classroom. The University of Maryland has thoughtfully chosen to provide Stafford and PLUS Loans through the FFEL program because of the value added services provided to our students. Our guarantee agencies provide educational information to our students on default prevention, debt management, identity theft, and financial planning, to name a few. With continual and consistent communication, students understand the impact of borrowing, and the consequences for non payment. This knowledge gives our students life skills they will utilize long after they receive their diploma. Because of our partnerships with FFEL lenders and guarantors, our default rate has dropped consistently over the last seven years. In 2000, our default rate was 2.6%; in 2006 it was 1.2%. For University of Maryland students who borrow utilizing American Student Assistance, the default rate is .6%.




Cohort Default Rate

| Year | Cohort Rate |
|---|---|
| 1999 | 2.50% |
| 2000 | 2.70% |
| 2001 | 2.30% |
| 2002 | 2.00% |
| 2003 | 1.70% |
| 2004 | 1.80% |
| 2005 | 1.20% |

The University of Maryland could not have provided those incredible repayment percentages without the assistance and knowledge of the lending experts. Since schools may face sanctions if their cohort default rates exceed certain levels, a lender and guarantor's effectiveness in working with borrowers to ensure that loans are repaid is a viable consideration when an institution chooses a loan program. Further, last year I decided we should conduct one-on-one counseling for students who reached a specific threshold of indebtedness per grade level. Our lenders very quickly were able to run reports for us to assess the indebtedness of our students. By profiling our students and providing them with individual counseling, we are able to further advance the mission of the University in educating our students.

In summation, we need to take steps now to prevent the disruption to the FFEL student loan program. We need to assure our students and families that student loans have been, and will continue to be, a resource for them. I thank you for having me speak with you today.

**STATEMENT OF CHARLIE C. SANDERS, JR., PRESIDENT AND CEO, SOUTH CAROLINA STUDENT LOAN CORPORATION**

Mr. SANDERS. Mr. Chairman and Ranking Member McKeon and committee Members, thank you for inviting me to come before you and for holding a hearing to discuss this very important issue. Prior to my role at South Carolina Student Loan, I was a municipal bond trader in the securities industry as well as director of investments and debt for our State Treasurer.

South Carolina Student Loan was created by our general assembly in 1973 as a nonprofit private entity. And since our inception we have provided nearly $7 billion in higher education loans to over 423,000 families throughout our State. Our nonprofit mission is to provide programs of financial assistance to enable students to pursue and achieve their educational goals. Without this financial assistance, families in South Carolina would not have been able to pursue their education dreams.

For the current academic year alone, we have provided over $600 million in loans, of which $63 million are private loans. I can tell you the current market situation has had an impact on our ability and that of my colleagues in other States in securing the necessary financing to provide student loans. The problems in this market are not due to credit risk but, rather, liquidity concerns. To repair the marketplace it is necessary to inject liquidity and restore confidence, and our Federal Government has this ability.

In South Carolina we have almost $3 billion in outstanding student loan bonds. And of that, approximately 60 percent are in auction rate bonds. In February the auction rate market collapsed. And in South Carolina alone, we have had 28 failed auctions just over the past several weeks. And we are now having to pay rates of more than 7 percent as compared to 3 to 4 percent just a short time ago. Some of my colleagues in this market are paying rates as high as 18 percent at a time when the statutory yields we earn on FFEL loans are roughly 4-½ to 5 percent. Therefore, most lenders are experiencing a negative return on their funds.

Because of this situation, we in South Carolina have been attempting to refinance our auction rate bonds into some other form of financing vehicle since October, and it usually takes about 2 months to do a financing. But we have experienced difficulties in securing this financing due to the apprehensive position of rating agencies, liquidity providers and investors.

The uncertainty of financing creates a situation where my organization and many of my peers are unable to commit to funding the same volume of loans we have in the past, if any loans at all. It has been reported that several lenders have suspended new loans, and I expect to see more announcements unless the financing situation improves substantially. This will certainly create access issues. The current market situation directly affects what we can do to serve students and families in our States. The FFEL public-private partnership has served students and families well for over 40 years and provided critical services.

If my organization ceases to be a partner in the FFEL program, services provided by our 230 dedicated and service-minded employees would be unavailable to our citizens. These programs include

financial literacy, college and career planning, debt management, as well as teacher and military forgiveness programs.

We are also partnering with our State Department of Education and several other State agencies in sponsoring an education and workforce development Web site serving over 600,000 students and a drop-out prevention program at 16 of our secondary schools.

Much has been discussed about a Lender of Last Resort program being the solution. It is not in my view the answer to this issue, as it is a capital markets problem and the Lender of Last Resort does not solve these issues. Instead I believe the most seamless solution for students, families and schools is limited and timely Federal financing to help restore confidence in this market.

The Federal Reserve took action just this week for the purpose of injecting both liquidity and confidence into the mortgage market. It is also appropriate for the Federal Government to take necessary steps to restore stability in this market. Therefore, I respectfully ask the Secretary of Education to continue to monitor the situation and review access issues using authority currently available.

At the same time it would be prudent for the Secretary of Treasury to take action as requested by many Members of Congress, including my Representative, Congressman Wilson, and others on this committee, to serve as the backstop for auction rate bonds and provide financings which would restore stability and confidence in this market. If action is taken immediately to address these issues, we may be able to avoid the possible shortage of funds for this next academic year.

Thank you for this opportunity to address you and I will be happy to answer any questions.

Chairman MILLER. Thank you very much.

[The statement of Mr. Sanders follows:]

**Prepared Statement of Chuck Sanders, President and CEO, South Carolina Student Loan Corporation**

*Introduction:* Mr. Chairman, Ranking Member McKeon, my name is Chuck Sanders and I am the President and CEO of the South Carolina Student Loan Corporation. Thank you for inviting me to come before you and for holding a hearing to discuss this very important issue—ensuring the availability of Federal student loans for students and families both near and long term.

Prior to my role at South Carolina Student Loan, I was a municipal bond trader in the securities industry as well as Director of Investments and Debt Management for the South Carolina State Treasurer's Office. Thus, I have long term experience in both student loans and municipal financing. I would like to tell you a bit about our student loan program in South Carolina.

The South Carolina Student Loan Corporation was created by the South Carolina General Assembly in 1973 as a private, non-profit entity to administer the Federal Family Education Loan (FFEL) program in South Carolina. Since our inception, we have provided nearly $7 billion in higher education loans to over 423,000 families throughout the state of South Carolina. Our non-profit mission remains unchanged—to provide quality programs of financial assistance that enable eligible students and parents to pursue and achieve their educational goals. Without such financial assistance, families in South Carolina would not have been able to pursue their postsecondary education dreams. For the current academic year (2007-08), we have provided over $600 million in educational loans.

As a not for profit student loan provider and issuer of student loan bonds, I can tell you first hand the impact the current market situation has had on our ability, and that of our peers in other states, in securing the necessary financing to provide access to student loans. While the immediate issue is that of a skittish credit market and the need for liquidity and confidence to return to the market, the implications go beyond direct financings. It is important to note that the situation we find ourselves in is a collateral affect of a much broader credit market disturbance insti-

gated by activities in the sub-prime mortgage market. It is not because student loans were poorly underwritten or issued to ineligible or undeserving borrowers. Furthermore, the credit quality of this asset remains high. The problems in this market are not due to credit risk, but rather liquidity concerns. To repair the marketplace, then, it is necessary to inject liquidity and restore confidence. The Federal Government has the ability to help stabilize this irrational marketplace.

As you know, we provide a myriad of programs and services for students in a holistic approach to assisting students and families. Much of this is also at risk if the current market situation does not turn around. I will discuss that more directly later in my testimony.

*Issues in the current market:* In South Carolina, we have about $3 billion in outstanding student loan bonds and of that approximately 60% percent are in auction rate bonds, with the remainder in longer term variable rate securities. Currently, across the broader student loan market, industry reports indicate that of the roughly $350 billion in outstanding FFEL program loans, about $80 billion are financed via outstanding auction rate securities. Most of this auction rate debt was issued by non-profit lenders, because this mode of financing was our best option to keep borrowing costs low. It worked well for 15 years in providing us with a consistent and predictable source of low-cost capital.

Late last year, it became clear that the problems in the sub-prime mortgage market were having a negative ripple effect on the student loan capital markets. Initially, this meant a significant increase in financing costs, but the market remained intact. In the second week of February, however, the auction rate market collapsed when broker-dealers—who have their own balance sheet issues—were no longer able to sustain the market by buying all the student loan securities that investors wanted to liquidate. Consequently, a raft of auction failures occurred, as sell orders vastly outpaced buy orders. This meant that some buyers had to hold the asset and were unable to sell for cash. This was a crushing blow, since the investor base for these securities existed because the asset has always been viewed as highly liquid. Once liquidity was no longer assured, many of these historic investors no longer saw a reason to be in the market. That investor base has yet to be replaced, and may never be replaced. Thus, the student loan auction rate securities failure rate has in a relatively short time gone from zero percent to nearly 100 percent.

In South Carolina, we have had 28 failed auctions over the past several weeks and are now having to pay rates of more than 7 percent as compared to 3 to 4 percent just a short time ago. Some of my colleagues in this market are paying rates as high as 18 percent, at a time when the statutory yields we earn on FFEL program loans are roughly 4.5 to 5 percent. Several news reports have described how individual nonprofit lenders are losing millions of dollars on their loan portfolios each month. The point here is that many lenders are seeing a negative return on funds and they do not have other sources of capital to draw upon. This means that they can only continue under current market conditions for a circumscribed period of time. While this time period will vary for each lender, the basic dynamic is the same.

Because of this situation, we at South Carolina have been attempting to refinance our auction rate debt into another financing vehicle since October. We are experiencing difficulties in securing this financing, however, due to the apprehension of rating agencies, liquidity providers and investors.

In the meantime, the uncertainty concerning whether these refinancings can be accomplished—and at what price—creates a situation where my organization, and many of my peers, are unable to commit to funding the volume of loans we have in the past—or in some cases, any loans at all. Recently, of course, it was reported that the Pennsylvania Higher Education Assistance Agency and others have suspended new FFEL program loan originations, and I expect to see more such announcements in the coming months, unless the financing situation improves substantially.

*Impact on Students and Families:* Without some relief to this situation, I believe you will see additional loan providers reevaluating their participation in both the Federal and non-federal loan programs. This will undoubtedly create access issues for some in both the FFEL program and non-federal lending. The South Carolina Student Loan Corporation provides both FFEL and non-federal loans. For many students, borrowing to finance their education is something they must do and we want to provide low cost loans to assist those students and families that need this assistance. We always encourage Federal and State grants and scholarships first. For some students, however, the non-federal loan is necessary to bridge the gap between federal loan limits and their cost of attendance. Both FFEL and non-federal loans are at risk due to this current market situation. While private lending has received

some criticism, it often makes the difference between the dream and the reality of a higher education.

While disruption may not be widespread initially, the potential is there for many more students to soon be without their provider of choice. To this point, students and their families have benefited greatly from being able to shop around and find the best deal possible to them for financing their education. There are also genuine access concerns. Many students may soon be without access to non-federal loans that they need to fill the gap left by federal loan limits. And access to even FFEL program loans will become a greater concern with each passing month that the market remains in its current state.

The current market situation directly affects what we can do to serve students and families in our states. The FFEL program has served students and families well for over 40 years. The public-private partnership has led to innovation and commitment by loan providers to supply low cost loans and critical services that help students pursue and complete a higher education. While we can do little or nothing about college costs, we can ensure students have efficient and low cost financing alternatives, and many other services to meet their needs. If my organization ceased to be a partner in the FFEL program, not only would a local mission-based organization vanish and 235 dedicated and service-minded employees be out of a job, but critical services would also be unavailable to our citizens. These include financial literacy programs, college planning, career planning, outreach, debt management programs, teacher and military loan forgiveness programs, and training opportunities for higher education professionals, to name a few. Our organization in South Carolina is both required and honored to serve students at every school in our state. Our absence would likely produce a disparate impact on different institutions within the state, with students at some schools facing a greater restriction of choice than their peers at other schools.

Much has been discussed about the Lender of Last Resort Program being the solution. It is not, in my view, the answer to the issue before us. This is a capital markets problem and the Lender of Last Resort does not solve the market problem to ensure students continue to have choice in financing their education. The situation in which we find ourselves is not loan providers being unwilling to provide funds to students, it is loan providers being unable to provide loan funds due to the liquidity issues in the market place. While it is prudent for the Department of Education to review current law and its administrative processes, it is far more prudent for us all to work together to do all we can to make sure such a drastic measure is not needed. Students should be able to continue to choose the loan provider of their choice, as choice is a fundamental tenet of the FFEL program. We want to work with the Congress and with Treasury and other Federal agencies to avoid a widespread disruption in both the federal and non-federal student loan programs.

*Ensure Choice:* The title of this hearing is ensuring the availability of Federal Student Loans. Along with availability, it is important that schools and students continue to have choice in meeting their higher education financing needs. These programs have become more effective overall by allowing choice. Colleges and universities are in the process now of packaging financial aid for the upcoming academic year. We should not ask institutions that have selected the program that best fits the needs of their students to completely change midstream. It is both necessary and possible to do what is necessary to find a common solution to the market issues before us. FFEL program borrowers may have already chosen their loan provider and requiring a move to the Direct Lending Program will be thwarting that choice. Students, parents and institutions are better off with the ability to work with the local, community-based or national organization they desire. If the Direct Loan program is indeed their choice, it should be for reasons other than having no other option at all. While Direct Lending may be the choice of some, it is not for all and we should be putting students first and shoring up their ability to finance their education in a manner that best meets their needs. We want to continue to work with our partners in the higher education financing community to provide the means for students and their families to pursue their education without concerns regarding student loan availability.

*Conclusion and Recommendation:* It is clear that this situation is not a byproduct of poor credit quality or flawed underwriting. Issuers are in this position due to no fault of their own, but rather as an unintended consequence of a larger market issue. I believe strongly that timely and limited federal intervention is warranted in this case to restore confidence in this quality asset and the student loan marketplace. The Federal Reserve took action just this week to inject both liquidity and confidence into the mortgage market. It is similarly appropriate and justified for the Federal Government to take the necessary steps to restore stability in this market.

Such measures would have positive, immediate and far-reaching implications for students, families and our country.

Therefore, I respectfully ask that the Secretary of Education continue to monitor this situation, utilize her existing authorities, and review access issues facing students across the country. At the same time, it would be prudent for the Secretary of Treasury to take action, as requested by many members of Congress, including Representative Wilson and others on this committee, to serve as a backstop for auction-rate bonds, making clear the Government's commitment to students across the United States. Finally, I ask that members of this committee work with their colleagues on other committees of jurisdiction.

We need to restore not only confidence in the markets, but also the confidence of students, institutions of higher education and student lending partners. In the spirit of cooperation, we can work together during this unexpected and extraordinary time to do what is necessary and what is right. Action taken immediately to address these market issues could prevent a potential shortfall of loan funds to students for the upcoming academic year.

I thank you again for the opportunity to address the Committee and appreciate the willingness of each of you to be here to take the time to hear from me and my colleagues about this most important issue. I am happy to address any questions you may have.

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Chairman MILLER. Thank you to all of you. You have all raised I think very important issues and from an array of perspectives. I think it is helpful to the committee.

Ms. Muilenburg, let me, if I might begin with you, thank you for your testimony and certainly for your written testimony as it is laid out. A number of us asked the Secretary about what she has been doing with respect to the guaranty agencies. Apparently there has not been a face-to-face meeting; is that correct?

Ms. MUILENBURG. That is correct.

Chairman MILLER. Your contact with the Department has been what? I don't mean you, I mean the agencies.

Ms. MUILENBURG. The agencies individually have contacted the Department to offer to come in and sit down. The President of our trade association, the National Council of Higher Education Loan Programs, has repeatedly offered to the Department to bring in a group of guarantors. We would bring in the chief financial officers, the operational folks, that would be able to sit down and talk about how to implement a program. The response thus far is they have appreciated the offer of assistance, they are monitoring the situation, and they will be in touch.

Chairman MILLER. As I understand it, in 1998, what was done is the agencies and the Department were brought together and they worked out essentially a legal agreement for how they would then proceed if necessary, and it turned out not to be necessary. But no such agreement has been suggested here to date?

Ms. MUILENBURG. Not thus far, sir.

Chairman MILLER. Is that agreement—or maybe your attorneys want to answer for the record—but I mean, is that agreement essential to proceeding?

Ms. MUILENBURG. It is essential if we are going to have to proceed using Federal advances. That was the—the key difference between the way the Lender of Last Resort program has worked to the extent it has been utilized in the past is it has been on an individual basis where there are students at a particular school in isolated circumstances who have not been able to get loans. In each of those cases guarantors have been able to find lenders to make those loans which would be considered——

Chairman MILLER. Those were very small. Mr. Wozniak and Mr. Sanders suggest that this problem is not one of isolated individual cases.

Ms. MUILENBURG. That is right. I mean, in USA Funds' case, we have guaranteed $1.8 million in Lender of Last Resort loans, the last being in 1998. And in all of those cases we were able to find lenders that would actually make those loans and we stood behind them as the guarantor.

But if we are talking about a much more widespread access problem, clearly Federal advances will be necessary, because the lending partners to whom we turned in the past to make these loans are obviously the ones that are potentially having the problem accessing the capital markets.

Chairman MILLER. Well, it is very disappointing to hear that that outreach by the agencies is essentially—I don't know if it has been rebuffed or ignored, but it hasn't happened. And I think we heard here, from members on both sides of the aisle, we are trying to have confidence that this system will be operational, if necessary. So I appreciate your testimony. I will come back to you.

Mr. Wozniak, Mr. Sanders outlined his living with—and I have two sons who are University of South Carolina Gamecocks by the way—he is living with what you described in the auction market. He has also suggested that if the Fed thought this was good for home mortgages, why wouldn't they consider it for student loans? He describes that as—and I think you did also—that this is a liquidity problem. People who thought they were going to be able to go and sell these assets and become recapitalized, liquid, to make additional student loans have now found out that that market has been closed to them, as apparently it was closed to municipal markets and utilities and the Port of New York and New Jersey and others. So this is spread across good paper, so to speak.

Do you want to comment on what Mr. Sanders said?

Mr. WOZNIAK. I think that is correct. And that is one thing over the—one thing to recall as we look through this is that the underlying collateral, the students themselves and parents, have actually—there has not been a material difference in how the payment has been coming in. So it is not a widespread subprime issue. It is actually the case that the collateral has been there performing in a very reasonable fashion.

So it is more of a liquidity and confidence issue in this process, which would hopefully be easier to work ourselves out of because we have collateral that is favorable collateral. It is just that in this type of market scenario it is more difficult.

Chairman MILLER. But in this market, I mean that collateral, 97 percent guaranteed, is treated——

Mr. WOZNIAK. Well, you know, there is the guarantee side and there is the spread side. And the situation is that because interest rates have risen so high that is the difficulty.

Chairman MILLER. That is the 100 basis points that you talked about?

Mr. WOZNIAK. That is correct. It would require far too much collateral. It is kind of like the old joke of how do you get $1 million from the stock market.

Chairman MILLER. Mr. Sanders has suggested what we have been talking about to date is that we are preparing a standby authority so that we have, as we understand it, we have access, or the Secretary would have access to the Treasury. He is suggesting that if you went out and purchased some of those loans, that these entities that have traditionally provided the loans for FFEL would be able to recapitalize some portion of that.

Mr. WOZNIAK. If there is some means, right. If there is some type of means providing some type of liquidity process—and that could happen in a variety of ways—that would help free up the market; that is correct.

Chairman MILLER. Does that have an impact on the timetable in which the credit markets might come back to something that we saw as normal, or is the auction market gone?

Mr. WOZNIAK. The auction market has—at this point it can—the auction market has always operated in a tremendous way on confidence. And from a confidence standpoint I would say that when you look at all the auctions that have gone before, and they had all gone fine, and the fact that—and it has even gone through some very difficult times and was able to be resilient. At this point it would be, I think, each of the issuers—virtually every issuer that I know wants to get out of them, and they are not necessarily looking at using that as a financing tool.

Chairman MILLER. Okay. We will come back to that in the next round.

Mr. MCKEON. We have a vote on, but we are going to take Mr. McKeon's line of questioning and then I think we will see what time it is.

Mr. MCKEON. Thank you, Mr. Chairman.

Mr. Wozniak, do you believe that we have a crisis on our hands when it comes to ensuring that all students will be able to obtain enough loans through the Federal and nonFederal bank-based programs to pay for college next year, and why or why not?

Mr. WOZNIAK. I would say yes, we have $80 billion of outstanding auction securities that issuers are trying to refinance. There is probably another $70 billion of loans that are sitting in the short-term facilities I was talking about. That is $150 billion backlog. And it is one of those situations that if your house is on fire you need to kind of fix that before talking about the addition.

So as you look in the current process of how to provide, it would seem that there is likely to be, when you look at the, facts some type of access issue if everything stays where we are.

Mr. MCKEON. Thank you.

Mr. Sanders, have you had to scale back any of your borrower benefit programs or value-added services that you provide to students or schools, and can you describe what has been scaled back and what led you to that point?

Mr. SANDERS. Yes, sir. We have actually already changed our borrower benefits related to our consolidation loans. We are making very few consolidation loans at this point. Also in the private loan part, we actually are having to increase our credit standards to have higher-quality loans which actually will reduce our volume roughly 20 percent. And we are also raising the interest rates on those private loans.

The reason for doing that is if the markets do recover at some point in the future, we are going to have to have higher credit standards in our portfolio in order to finance it. So, yes, sir.

Mr. MCKEON. Thank you very much.

Ms. Bauder, in your testimony you had mentioned the administrative costs associated with updating your preferred lender arrangements and staying on top of what lenders are still in the program. Given those additional costs, why will you choose to stay in the FFEL program rather than switch to the DL program?

Ms. BAUDER. Two main reasons. One is the mission of the university is about education. Our president continually says regardless of whether you are in the classroom or whether you sit in an office, you educate students. And so to that end, we partner with vendors and guaranty agencies that have that same mission in mind.

You know, student loans are usually the first time a student has an introduction to debt. And so when you are thinking about debt, you have to think about it in terms of a life skill. What are we teaching them from the moment they borrow to the moment they are actually done repaying? And so if we think about student loans only as receiving a check, then we minimize the entire program. It is important we want to get our money.

I think Roberta was talking about the ease of the direct lending program. I will mirror that with FFEL. It is an incredibly good culture to be in. We have 1½ employees that operate the FFEL program. To switch into direct lending is not an easy switch. We are talking about a culture here. We are talking about system changes. It would take us probably a year so that it would be transparent to the student to move over into direct lending. We would have to notify our software providers what we are doing. We do do PELLs and we do have COD, Common Origination and Disbursement, as Roberta was talking about, but it is not an easy switch. Communication on the Web. I mean I could go into my—put my operational hat on and give you the numerous amounts of if we didn't do it correctly, the disruptions that would fall onto the student. But the main thing is we really want to educate our students.

Our default rate has gone down significantly because I am able to pick up the phone and call a guaranty agency or a lender and say, I want to profile my students; could you tell me for all of our sophomores if they are at a $15,000 indebtedness, I would like to know their names. I don't have that capability on campus right now to do that. So they can do that.

We can call them in on a one-on-one basis and start counseling them and say, Do you understand this is the repayment you are going to end up with? Do you understand the difference between a want and a need? Are you really borrowing what you need or are you borrowing for something else? That is important. That is a life skill that we are training our students on so that when they exit, you know, when they get a car, a mortgage, or a credit card or whatnot they are actually planning for their future.

Mr. MCKEON. That brings up a point that I have been very concerned about. The Secretary said that she could probably double their capacity. So if they are doing 20 percent of the loans now, they could probably double that. I don't know if they meant they

could do that by next summer or fall, or if it will take a year or two. The problem is right now. It may fix itself next year.

I mean, liquidity confidence could come back in maybe. Sometimes an election gives people new change, new start. It builds up confidence. But I am concerned about next summer and fall. And if it takes a year to switch to direct lending and if you have a lot of schools trying to do that all at one time, I am very concerned about the Department's capability of handling that.

So thank you all for being here and for your testimony. I think this has been a very good hearing and I think it is very timely, very important, and I hope it causes some real focus on the potential problem at hand.

Thank you Mr. Chairman.

Chairman MILLER. Thank you. I think—I mean, we will go back and look at the Secretary's testimony. I think it was she could double it relatively quickly, I mean like overnight. Beyond that was a longer time.

Mr. MCKEON. She didn't say a time.

Chairman MILLER. Well, we will ask the Secretary for clarification, because it is very important to this hearing whether or not she has the capacity to do that, to go from 30 percent to 60 percent or whatever, and in what time frame. Again, that is what we are trying to sort out in this hearing.

We are going to go vote and we are going to recess here for a few minutes, and then we will come back. Members expressed interest in asking questions and I have another round. And the challenge is, can I get to the floor in 36 seconds?

[Recess.]

Mr. KILDEE [presiding]. The committee will reconvene, and the Chair recognizes the gentleman from New Jersey, Mr. Andrews.

Mr. ANDREWS. Thank you, Mr. Chairman. Thanks to the panel for your outstanding presentations and for your patience in waiting for us to get back. Thank you very much.

I have heard some points of consensus here this morning. One is that we want students to borrow less and get more scholarships. I think we all start from that. The second is that we want a healthy FFEL program and a healthy Direct Loan program. And the health of the FFEL program I do think depends upon a ready and willing and able Lender of Last Resort. We have got to get that in gear if it is needed on a large scale.

And then I think it is also a consensus that students who have not yet exhausted their Federal resources to go to school, and have a gap, should exhaust their Federal resources. We should educate them about that and let them know before they go into the private loan markets.

But we do have a situation where a significant number of students after they have exhausted those Federal resources, after they have gotten all the scholarship aid they can, have a significant gap.

And, Ms. Bauder, I think you have given us a great example of that in your written testimony where you hypothesize a first-year student at the University of Maryland, State resident, no parental contribution, and he or she would be $3,608 short of the package that they need.

I think you can tell that story about a student at a NAICU private college or university where the tuition is probably twice as high. You can tell that story about a student at a career school or technical program where you have high tuitions very often as well.

What ideas do the members of the panel have as to how we should approach that problem? And, again, I am hypothesizing, the student who has exhausted their scholarship aid, exhausted their Federal resources, has a gap between the money they need and the money they have and has to turn somewhere. My sense is that they are the classic subprime borrower, that the prospect of attracting private capital for them is a very difficult prospect indeed.

And also, I think I have this right, and I think the Secretary may have inadvertently stated this, we can get the Lender of Last Resort program 100 percent right, but it doesn't change the loan limits, right? You can go as high as you go, and that is it? So what ideas do the members of the panel have for us as to how we can address the needs of that student.

Ms. JOHNSON. I think one of the issues was one that Sarah alluded to in her testimony. And that is the fact that with the Federal Perkins loan program we are seeing some drastic reductions on our campuses as a result of a couple of different things. One is that the influx of cash that we experienced into our revolving fund as a result of consolidations is dried up, because there is really no need for students to do a consolidation anymore when the interest rate on the Stafford loans is higher than what it is on their Perkins loan.

Mr. ANDREWS. I completely embrace that. If I were writing the budget myself, I would have a much higher level of Perkins number than we do. I think the reality is, there is a likelihood we will operate on a CR around here until there is a new President. I am not saying that is going to happen, but I bet it does. And that means we are going to be at something like the present level in Perkins, so it is not going to be a whole lot of new money in Perkins. I wish that weren't true but I think it is. So what else do we do?

Ms. MUILENBURG. I think you probably have to think at this point about increasing loan limits. It has been under discussion in previous higher ed bills, and it hasn't been done I think largely due to cost considerations.

Mr. ANDREWS. How do we pay for that?

Ms. MUILENBURG. Well, you could add unsubsidized loan eligibility, which my understanding is not a cost item in either FFEL or direct lending, and to provide some additional capacity.

Mr. ANDREWS. I am not sure about that. I think that it is not subsidized in terms of the outlays, but if there is a guarantee attached to it. Are you proposing a guarantee be attached to it?

Ms. MUILENBURG. That it would be available in both programs.

Mr. ANDREWS. Well, I think CBO would attach a number to that. So assuming it did, where do we look for resources to pay for an extension of loan limits? Welcome to the Congress.

Ms. MUILENBURG. I fully understand. We are well aware of the cost constraints that you all face.

Mr. ANDREWS. And you do understand one sort of arcane technical point, but it is a very big deal. The way things work around

here is if we look for offsets, we need to find them within our own little universe here of programs. And we really only have three things. We have the Pension Benefit Guaranty Corporation, we have the School Nutrition program and we have student loans and that is it. And we can't take the money out of the Iraqi budget surplus. They have a budget surplus in Iraq. We can't take it out of agriculture. We have to find it within the four walls of our own jurisdiction, which is not easy.

Ms. BAUDER. Could we talk about ACG, SMART and TEACH?

Mr. ANDREWS. I'm sorry, could you put your microphone on? And my time is expired.

Ms. BAUDER. So I can't?

Mr. ANDREWS. Well, I am sure the Chairman will let you quickly answer the question; not to speak for him, but may she answer my question?

Chairman MILLER [presiding]. Sure.

Ms. BAUDER. Okay. Thank you. ACG, SMART and TEACH are very cumbersome and costly to administer. I don't know if there is any—and I am totally brainstorming—I don't know the back end of how all the financing works, but taking those funds and putting them back into a program that is very easy to administer.

Mr. ANDREWS. Which programs are you saying?

Ms. BAUDER. Academic Competitiveness grant, SMART and now the new TEACH program.

Mr. ANDREWS. If I can just bore you one more time with details. But I think most of those fall into what we call the discretionary spending world. I don't think they are mandatory. Am I right about that? Okay, well, that gives us something. Although, you understand, one of the great glories of governing in tight fiscal times is that anytime you take a dollar away from one thing, you generate opposition to it.

But listen, we would welcome your ideas. It is a tough problem, but we welcome your ideas. So I think we all agree, as the Secretary said, we want to educate students to get every last Federal dollar for which they are eligible so they don't have to go to the private market if they don't have to.

Chairman MILLER. I think Mr. Sanders wanted to comment.

Mr. SANDERS. Mr. Chairman, I was going to say that if the Federal Financing Bank was to come in and do some kind of financing—currently they invest in Treasurys which are below 2 percent—but if they were to provide some type of financing based off, say, 3-month LIBOR plus a spread, they would be earning somewhere in the 3½ percent range. So it would not be a cost, it would be actually an earnings to the Federal Government.

Mr. ANDREWS. What default rate are you factoring in on that?

Mr. SANDERS. Those are with Federal loans I am talking about.

Mr. ANDREWS. Okay. I appreciate that thank you.

Chairman MILLER. Mr. Souder.

Mr. SOUDER. Thank you Mr. Chairman. I apologize for being late to the hearing. I was able to hear the original opening statements of Secretary Spellings, and all this panel's testimony, as well as your and Mr. McKeon's questions due to the wonders of C-Span. But in between there, I had the mayor of Fort Wayne, the newly elected mayor who was here for his first visit to D.C. since being

elected mayor, and we had a few things we needed to do that were local in addition to national.

But one of the things that came up that I wanted to ask Ms. Muilenburg—and if anybody else has any comment with this—there were some references made, but I missed some of the more intense discussion on this, in the first panel, of the difference in trying to account by university or college if they run into shortage of funds as opposed to systemwide.

As the Chairman knows and as most of you who follow the issue, I am a strong advocate for nondirect lending. I believe the private sector has gotten the loan rates down. I believe that they service the students better.

I thought Ms. Bauder did a terrific job in laying that out in hers, in trying to make sure that people and our students have access to education even with the uncertainties. And if we start to get in a pickle here, I don't want to have to throw out the baby with the bath water, so to speak, and have the Federal Government wind up at the end expanding their powers, to the disservice of students and the disservice of the taxpayers, because this system has worked better. At the same time, clearly the Federal Government may have to step in. And I was trying to sort through what did it mean precisely if they do it by college or university as opposed to systemwide?

Ms. MUILENBURG. What we were recommending, Congressman, is a system whereby a school would be able to be certified as a Lender of Last Resort school and that we would not have, as guarantors, to force students to go through the hoop of going to two lenders and being turned down by two lenders before being able to access an LLR loan.

So the concept would be an institution-wide eligibility for Lender of Last Resort services. And, clearly, in the situation where there would be a widespread access, we would need Federal advances in order to make those loans available. Does that answer your question?

Mr. SOUDER. I believe so. I want to do a follow-up with Ms. Bauder. When you were talking, you said about the difficulty, and then it came up, the question of if all of a sudden people switched. Would the doing it school by school resolve some of that question? In other words, at least it wouldn't force everybody into that type of system. How do you see that playing through in regards to your concern of the difficulty in making a fast switch?

Ms. BAUDER. I like the option of Lender of Last Resort being an umbrella over the school. Is that what you are—yeah, I think that is a good option in terms of—rather than having the students jump through so many hoops on an individual basis. Going into direct lending is somewhat cumbersome. It is a culture.

It would be an easy switch if we didn't care about the impact on the student. We can transmit anything and create systems. But what it does is, there is a disruption to the student in terms of process, having to do another MPN, just the entire culture of student loans. And so in order to make that transparent and seamless for the student, it is somewhat cumbersome.

Mr. SOUDER. Ms. Muilenburg, if it went by school, would that make it easier for the private lenders to step back in after the credit crunch occurred? What would the transition back out of that be?

Ms. MUILENBURG. The situation that we would envision working, and obviously we would have to sit down with the Department to figure out all of the operational details, but the notion would be that for as long a period as was necessary for the school to participate in a Lender of Last Resort program, that they would be able to do so, where the guarantors would essentially be the lenders as well as the guarantors of those loans.

But certainly if the credit crisis begins to resolve itself, then there would no longer necessarily be a need for that school to participate in a Lender of Last Resort program. If the lenders with whom they have worked over the years reenter the marketplace and are able to make loans, we would certainly anticipate those schools returning to a normal FFEL loan processing environment.

Mr. SOUDER. There seems to be a general concern in both parties that the administration wasn't doing a lot of advance planning regarding if the situation really turns bad. I know a number of members were asking questions, but I didn't get to hear Secretary Spellings' response. Have they talked to you much about this? Are they very far along in this plan? Do they seem locked into a different alternative?

Ms. MUILENBURG. The Secretary indicated this morning that they intend to issue guidance to the guarantors, I believe, next week. And that is both heartening and disappointing news. I am heartened that she is going to issue guidance about the program and how they would anticipate it working. It is disappointing that she didn't have her staff sit down and consult with us beforehand in order to make sure that operationally it can work.

Hopefully it will be, as she indicated, an iterative process where we can work back and forth to figure out what the best way is to make sure that it works operationally smoothly for schools and students.

Mr. SOUDER. "Disappointing" is a rather understatement.

Chairman MILLER. Mr. Kildee.

Mr. KILDEE. Thank you, Mr. Chairman.

Ms. Johnson, you talked about the importance of helping students and families understand their options for Federal student aid and the differences between Federal and private loans. How do you do that and how are you helped by the Department of Education in doing that?

Ms. JOHNSON. Well, one of the things that we do is we encourage all of our students, obviously, to complete the free application for Federal student aid, and we do that relentlessly and through a variety of mechanisms: sending e-mails to currently enrolled students; sending correspondence to prospective students; sending postcards home that their parents might read, because we really want everyone to complete the free application for Federal student aid.

Our profile is very similar to Ms. Bauder's in terms of the number of students who do complete the FAFSA form and how many are ultimately packaged with student loans and how many of them ultimately will go about securing those student loans.

The other thing that in our environment has been very helpful is that because we are a Direct Loan school, my staff is freed up to spend time with those students. Our experience has been that students who are having questions about how to fund their education come first to the financial aid office. And when we would previously have to say well, you need to contact your lender about that, the response that we were getting from our students was, You are just giving me the runaround, you can't handle my question. You have to go someplace else.

And my staff is trained now and they know with certainty when those dollars are going to come in and we spend time—we have the time to spend with those students to counsel them about the difference between a subsidized and an unsubsidized loan, about taking a Federal loan versus taking a private loan. And parents are always asking us, if they are looking at a private loan, they are looking for us to give them recommendations as to which private loan they should even take. And ultimately that cannot be our decision to make for them. They need to make that choice based on what is best for that particular family.

But it has afforded us the opportunity to be able to sit down with those students and their parents and say, here are your options, here are things that you need to think about as a student and as a family, but you will need to make the selection, if you are particularly needing to use a private loan, because you need to choose a product that is going to meet your circumstances.

Mr. KILDEE. Do you think that the Department of Education could do much better itself in trying to assist these students in making these decisions?

Ms. JOHNSON. My experience with working with the literature—and they do put out some very fine pieces with literature—is that students and their parents, and maybe it is a culture of students that are used to instantaneous and video and multimedia ways of getting their information—but that many of our students are not utilizing the written documentation that the Department of Education is providing.

So that the opportunity to sit down one on one or provide information to them in other formats is very helpful.

Mr. KILDEE. Thank you very much, Ms. Johnson.

Chairman MILLER. Mr. Payne.

Mr. PAYNE. Thank you very much.

A question. Two questions. But the first one is even if the Federal Family Education Loan, the FFEL, or the Direct Loans are available, how will students be able to finance a gap between what the Federal student aid covers and the total cost of education today?

In other words, saying that the Federal Family Education Loans or Direct Loans are available does not mean that access to higher education is ensured particularly for lower-income students who want to attend private institutions. And I just wonder if any of you have any thoughts on that.

Ms. BAUDER. Well, I can look historically and say that the gap has been met through multiple resources. One is, most institutions have a payment plan. We have a Terp payment plan where you can pay out of your operational home budget once a month to make up

for that delta. Credit cards, home equity, retirement plans. There are multifaceted resources.

The home equity now. I mean, a lot of the homes where last year parents had equity to borrow from, obviously that is no longer there for a lot of families, and so that resource is dried up. And in turn sometimes retirement as well.

So now we are stuck with, probably, credit cards. We actually are looking in terms of how are we going to advance our Terp payment plan, can we move it around a little bit to make it more advantageous for our families?

Mr. PAYNE. I hope they don't have to use credit cards, not the credit cards that I see interest rates floating around of 32 percent. Unbelievable.

Just a question in general. For example, there are some kind of unique programs that have been created by States for different purposes, perhaps. I know that Georgia started the HOPE loan, the HOPE scholarship. And I understand that the purpose was supposedly to keep top Georgia students in Georgia. In other words, they didn't want them to go out of state, they wanted them to stay in State. They needed an incentive to keep them in State, so that they would stay in State.

And the program is funded through the lottery, where mostly low-income people, unfortunately, are hoping—maybe that is why they call it the HOPE scholarship—they are hoping to hit the lottery, and many times don't. The ones who can least afford it are doing the lottery.

What happens is that minority students you get in, if you have a certain grade level at your high school. However, when you are thrown into the mix, in many instances because of the inequity in the educational level at the various high schools, those minority students in many instances—because you have to maintain a certain grade average—can no longer be allowed to have the HOPE scholarship and therefore have to drop out of school or go somewhere else.

Of course, the brighter students that they want to keep in are doing well because they would have done well anyway. Also students of wealthy people and people who could afford to pay are now getting a free pass. And those who need it the most are really losing out.

Now, I know none of you are from Georgia, but how do we kind of structure things so that they sound good—but, once again, it seems like the people that need help the most, even with these newly created programs, really tend to end up still at the bottom?

Do you think a program conceived like the HOPE program, you are in South Carolina, maybe do you have something similar to that, you are right next door, and how do you in your opinion—I am not knocking any of you because you are not from Georgia, and I wouldn't even knock a person if you were from Georgia, "Georgia on my Mind," you know, I like that song. But could you——

Mr. SANDERS. We do have a program in South Carolina that is funded by the lottery. And I will tell you, though, with North Carolina having created their lottery, just in the last year our revenues are down 100 million in our lottery program. So they are scrambling as well. We are facing similar situations to what you are.

Mr. PAYNE. One thing I do find disheartening is that too many States have decided to use the lottery for funding. In New Jersey the senior citizens PAAD $2 prescription drug benefits was paid for by casino gambling, because we have that in the State. Now Pennsylvania has casino gambling, Delaware has casino gambling, New York has casino gambling. And, of course, the revenues in casino gambling in Atlantic City are down, therefore challenging those programs.

So I just wanted to throw that out, because we really need to figure out a way to try to see that those students who have the ability to make it can. I won't get into endowments because we may be— I hope the Chairman has a hearing on that in the future to talk about universities that are sitting on hundreds of millions of dollars and students are unable to afford it.

Thank you. I will yield back.

Chairman MILLER. Thank you.

Terry, we talked quickly with the Secretary about the question of whether the Lender of Last Resort would be up and running so it could be done on an electronic loan processing arrangement. Mr. Warder suggested that that could be done. What do you know?

Mr. MUILENBURG. Well, we would certainly want to do it in an electronic loan environment, just the way we do all of our FFEL loans today. Back when the last Lender of Last Resort loan was guaranteed by USA Funds we could handle those on a manual basis, loan by loan. But certainly in a big situation, we would want to be able to use an electronic loan process. We are now going into our systems to identify the systems changes that need to be made to administer an LLR program and beginning to make those system changes today. The challenge, of course, is we don't know what the parameters of that program are going to be, whether there are going to be Federal advances made and how we need to set up operationally if we are going to be able to draw down funds to actually originate the loans. But we are doing everything we can to do the systems modifications today, to enable us to meet that need if it arises.

Chairman MILLER. Ms. Johnson and Ms. Bauder, Ms. Johnson, you are in the Direct Loan program——

Ms. JOHNSON. Correct.

Chairman MILLER [continuing]. So this is all interesting, I guess to you, but it is not urgent in the sense of your institution. Ms. Bauder, what is your sense here when you look down the road and you listen to this conversation? Will you wait for the Lender of Last Resort and just work through your guaranty agency, or would you apply for Direct Loans or not? What would you use as your standby if you think that we could go into July and August with a market in turmoil and lenders having trouble becoming liquid enough to meet that demand?

Ms. BAUDER. Well, I guess I would start by saying I would hope we would put more options on the table. I didn't come with any, but I would certainly try to think of other options besides direct lending and Lender of Last Resort. I unfortunately have only heard about Lender of Last Resort—I think yesterday is the first time I heard about it. And being in financial aid almost 20 years, it is a little nerve-wracking in terms of saying, hey, we are going to rest

our laurels on something that sounds as if it is not tried and true. And if I don't know about it, I am sure that other administrators are in the same boat that I am in. So I am not——

Chairman MILLER. That is why we are trying to encourage some communication here.

Ms. BAUDER. Exactly. So I don't have enough information to talk intelligently about it. Direct lending, again, I think we signed—I wasn't at University of Maryland when they originally thought about getting into direct lending. They did sign up for it, but I believe processed a few loans, but really just dabbled in it. And I certainly wouldn't want to go in that direction.

I do see, if you look historically that, you know, the FFEL program, our students really benefited from the subsidies in terms of having zero fees, having a lot of back-end benefits, having a lot of brochures and one-on-one hand-holding in terms of going through the process up through repayment. And so now I think those fees are going to have to—the student is going to take the brunt, eventually, of the pricing advantages that they had before, they are going to be charged those fees.

And so that is a concern of mine as I look down the road of saying—in fact, I think I have in my testimony the three things we look at when we look at our lender list is pricing, technology and customer service, and then mission with the university. This year I am not looking at pricing. I think we live in an unstable environment right now in terms of financing, and so we are looking at technology, customer service, and then mission with the university as we are looking forward.

Chairman MILLER. I understand that. And that is everybody's preference. We are talking about here, if in fact these lenders cannot get liquid enough—I mean, cannot recapitalize to get liquid, again that is all interesting, but they will not be available to make the loans. So I think what we are suggesting is people ought to start thinking about some standby, hoping they won't have to use it.

Clearly, the preference of this administration, and properly so, is the marketplace here. But so far that marketplace, as Mr. Wozniak has suggested, has not been able to untangle itself with respect to a whole range of credit instruments, whether it is municipal bonds or utilities or special local agencies, all of which have substantial streams of revenue, and highly rated and all the rest; when they come to the auction market they are treated as Mr. Sanders is, who never thought he would be treated in this fashion and has never been treated in this fashion by the auction market.

So this is about what happens in the event that—and then how you complete that sentence. I can't argue with your statement that probably most loan officers have not heard about it. There would be no reason to think about it in the historical performance over the last several years. Why would you think of Lender of Last Resort? But the mortgage lenders didn't think about the Lender of Last Resort, and the municipal bond people haven't thought about Lender of Last Resort. Nobody has thought about this until they get hit.

Mr. BAUDER. Right.

Chairman MILLER. And they have all been hit now. And it has turned out to be a rather dysfunctional market. And I don't want to put words in your mouth—I want you to comment—but you don't seem, Mr. Wozniak, to be confident that this is going to sort itself out anytime soon. Again, we are all open to we get a surprise every day here. Sometimes they are positive and sometimes they are negative.

Mr. WOZNIAK. No, from a standpoint the municipal market is certainly working its way through, and they have various streams. In the student loan market, we of course deal with a specialized asset that has a particular return. We don't get to establish what the interest rate is. And there is a tremendous amount of assets that have to be refinanced. So it is going to take some time. And even if rates come back tomorrow, they are not going to move back to where they were last summer in a straight downward pattern. So it is going to take some time as the market has to regain confidence.

Chairman MILLER. Do we have any way of inferring that if the infusion that we saw—was it $200 billion that the—was it $200 billion?

Mr. WOZNIAK. $200 billion, yes.

Chairman MILLER [continuing]. $200 billion that the chairman of the Fed put into the system, that that would have any spillover in a positive sense on those same institutions that are also lenders to the student loan market?

Mr. WOZNIAK. It may be too early to tell. The facility is a 28-day facility with extensions. Part of it, and what we are looking at in the current case with the auctions and others are much longer assets than that. Obviously, the mortgage assets are long-term assets, too. It is an attempt to put some liquidity in the system. It isn't going to be helpful directly to the auction market. I think that has a different component to it, different type of issue that is surrounding it, outside the overall securities markets in general.

Chairman MILLER. Mr. Sanders, if you can't go—you mentioned you had seen 28 failed auctions. If you can't go to the auction market, what is your anticipation of your situation?

Mr. SANDERS. Well, the situation we have with our failed auctions is existing debt.

Chairman MILLER. Right.

Mr. SANDERS. We are certainly not trying to issue more auction rate bonds at this point. But I think Paul is right; the situation with the Fed injecting money into the mortgage-backed system, certainly it is going to help in that market a little bit. But I guess the best thing that can be said about that is it wasn't bad news.

In our industry, pretty much every day has been bad news, so at least it wasn't that.

Chairman MILLER. What do you look to in terms of your ability to make these loans?

Mr. SANDERS. Currently, we are looking at trying to refinance into what are called variable rate demand bonds, which requires a credit facility, banks that would be standby in order to buy the bonds. You also have to have the rating agencies to rate the bonds. The process we have been going through for the last 4 to 5 months has just been a give-and-take. The rating agencies as well as the

credit facility banks are just nervous at this point. They continue to want more and more, and it is making it very difficult for us to get that issue accomplished.

Chairman MILLER. Okay. Ms. Johnson, Ms. Bauder talked about the consolidators who aren't available at the moment. Is your situation the same as hers or——

Ms. JOHNSON. Well, our students primarily will consolidate to the Federal direct consolidation program——

Chairman MILLER. Back through the program.

Ms. JOHNSON [continuing]. Directly into that program. So we have always suggested to our students that they do have choice on the back end with their student loans. And if they find a FFEL lender who would consolidate and offer them benefits that they find agreeable to them, particularly at the point of graduation when they know where they are going to be living and what their salary is going to be and what makes sense for them, that they should be looking at consolidation. But primarily our students have been consolidating into the Federal Direct Loan program.

Chairman MILLER. Has that changed? You were talking to a couple of other members, both of you, about the impact that has had on the Perkins, on the repayment. Is your outlook different than Ms. Bauder's?

Ms. JOHNSON. Our outlook is exactly the same as Ms. Bauder's, and primarily that is because of the interest rate change in the Stafford loan program. When it was variable with the cap and it was very low interest rates for a number of years, students who had large volumes in the Direct Loan program at very low interest rates were very eager to consolidate their loans and their Perkins loans with those, because it would draw down their overall interest rate on those loans.

Since that has moved to a fixed rate loan, those students are less likely to consolidate those loans. They would rather leave their Perkins where they are, at a 5 percent rate, so we are not seeing that infusion of capital.

I would like to also just address something that Sarah had talked about, and that was a little bit about the conversion into the Direct Loan program. And I hope I am not reading between the lines, but I thought I heard the Secretary this morning say something that they were looking at all options, one of which was looking at something with the transmission of information in the FFEL. And I believe that FFEL lenders are using a format that is called Common Line.

Several years ago, I think every school that was in the Pell Grant program was trying to convert over to a new schema called XML formatting. And many of us were not there yet in terms of doing that. And so for at least 3 or 4 years, the Department of Education had a conversion program that was available for us so we could transmit our Pells in our current school format. They would do the conversion into what the common origination and disbursement needed and then pass it back through the conversion box so that we could receive it back in a format that we could utilize on our campuses.

As I brainstorm about ways that perhaps some schools may find it easier to transition into the Direct Loan program, if such a con-

version box were available so that schools that are currently using Common Line could pass their current information through the conversion box that could be translated by the Department of Education to process those loans and then convert them back, I think that the up-front conversion time for the schools would be mitigated to some extent. Yes, students would have to sign a new promissory note, but for some students who are already possibly looking for a new lender they would be having to sign a new promissory note anyway. So it is something I think that they should consider.

Chairman MILLER. Thank you. That is why we are trying to encourage these conversations. Mr. Keller.

Mr. KELLER. Thank you, Mr. Chairman.

Twice during this hearing, a reference has been made to calling the red phone at 3 in the morning. If you are a student lender and you are calling the White House red phone at 3 in the morning, no matter who the occupant is, you are going to be in trouble. McCain is going to snap at you for making him talk about something other than national security. Hillary is going to hang up on you because she wants to put you out of business. Obama is going to politely call for change and hope, changing his phone number and hoping you don't get the new one.

The 80 percent of students who rely on the FFEL program for the Federal student loan program, I hope we have something better than a red phone strategy at the end of these hearings. My biggest concern, frankly, is outside the FFEL program for the students who utilize their FFEL loans as best they can, but the tuition gap is so huge they have no choice but to get the private loan.

And let me start with you, Mr. Wozniak. What impact on the students who are relying on these nonFederal private loans is the current credit situation likely to have?

Mr. WOZNIAK. Okay. Multiple issues are occurring I would say. One is that the cost of funds is higher, dramatically higher, no question about that. That means that that cost has to be passed on.

Number two, again, I think generally speaking again, the student loans process with regard to private loans performance has not had significant deterioration relative to over time. So it is a situation where it was not a big subprime type of activity. But nevertheless, the rating agencies in the current environment are re-stressing and adding more assumptions within their assumptions. So what is going to happen there is, there will be more protection that needs to be built into structures. Both of those items will tend to protect the bondholders more going forward, and will also result in a higher cost of funds to a smaller segment of students.

Mr. KELLER. Let me follow up your line of answer there. When you say higher cost to students, do you mean potentially higher interest rates and higher origination fees?

Mr. WOZNIAK. Yes to both.

Mr. KELLER. When you say the credit situation, you are going to have lenders requiring a better credit score from the students and/or their parents in order to qualify for a loan?

Mr. WOZNIAK. The cut-off rate, so to speak, will be at a higher credit score than previously.

Mr. KELLER. Is it possible that they may even start requiring some sort of collateral for these loans?

Mr. WOZNIAK. I don't—I would say no. That type of borrowing can be done—and again, I suppose through a home equity or other line to the extent that that was an option. But no, I would say no.

Mr. KELLER. Okay. And for the students who are from low-income families, 18-year old kid trying to go to college. And his mom, single mom, is a waitress, probably is not going to have a great credit score. What is their option going to be?

Mr. WOZNIAK. That again, from the private loan marketplace itself, is not for everybody. In part it is—in many regards that part of the market is hoped for, and I know there is only a limited amount of scholarship grant money and other types of funds. But the process is not to give somebody a loan if it is believed that they would have difficulty paying it back.

Mr. KELLER. Okay. Ms. Bauder, let me ask you a similar question to the last question I asked. What options do students have to pay for college if they have maxed out their Federal aid and are not eligible for a private nonFederal loan?

Ms. BAUDER. Well, we actually have students on campus like that today. Typically, we work with them on a case-by-case basis. Usually, we do some type of payment plan for them over time. Right now our payment plan is 8 months or 10 months. We will extend it through the summer and see what they can come up with. We also work with our development office to see what funds they have that are for need-based funding. But it is really on a case-by-case basis.

Mr. KELLER. All right. Mr. Sanders, you are a FFEL lender and you also provide private loans, is that right?

Mr. SANDERS. That is correct.

Mr. KELLER. Tell us what the current credit situation has done in terms of student options both under the FFEL—under the FFEL and the private lending. How has that affected students in a real world basis?

Mr. SANDERS. Well, I think as was mentioned earlier, we are really not into the loan season yet. We are probably about a month away. I think schools are probably in the process of packaging loans now. But as I mentioned earlier, we are actually tightening our credit standards. We are having to. We are also increasing the interest rate. And again, we are doing that because when we do exhaust the funds that we currently have, which will be sometime in the late fall, we will have to have better credit standards if we want to access the financial markets in the future.

Mr. KELLER. When you say you are increasing the interest rates, are you talking about on the private loans?

Mr. SANDERS. That is correct. Private loans only. On the Federal loans there has been no effect, and I am still hopeful there won't be any effect.

Mr. KELLER. All right. Thank you.

Mr. Chairman, my time has expired, so I yield back.

Chairman MILLER. Thank you. Mr. Souder?

Mr. SOUDER. I am kind of baffled about something here. This sounds like a one-way market. Normally, if you would have a tightening of the credit and inability to buy, somebody would start to

adjust the price. Are you suggesting universities aren't going to respond at all in trying to adjust tuitions? Is it just an inertia that in this country they can raise tuition indefinitely, regardless of whether students can afford to go there? If students start to drop off and not be able to go to school, Mr. Sanders, is one possibility that people will price-shop more for where they go to school?

Mr. SANDERS. You know, that is a good question. I don't think we have reached that point yet. Certainly I think that is a possibility. We obviously have a very good technical college system in South Carolina that a number of students are now starting to enter there for their first year to get their general courses out of the way, and then transferring later to our 4-year schools. So that is already occurring in my opinion.

Mr. SOUDER. My family didn't have enough money not to price-shop. We didn't have some kind of protection behind it. My dad had X amount. He said if I went to the regional campus and lived at home, he would work with grad school.

Are we trying to build a system that anybody can go anywhere they want at any time, the universities never have to adjust any tuition? I mean, I don't view it as a bad thing that there is some element of risk assessment here and repayment assessment.

Another concern I kind of had when I was listening to the discussion is that it doesn't seem—let me ask this question to Mr. Wozniak. Has the market so bundled—because there is a big frustration in the housing market of people who feel that their credit is being stressed when they weren't the people who took the balloon payments. Is there any kind of market mechanism that adjusts for those lenders who actually have the ability to get their loans repaid, did a wise job of estimating and balancing that, or are they just being bundled with high-risk loans and the market is going to dry up and change everybody's rates because there has been no risk assessment?

Mr. WOZNIAK. No. Again, the marketplace on the education loan side, again, has not seen any particular big jump up in any type of performance status. So the students are continuing to make their payments, lenders continue to work with students to make sure that they give them every opportunity that they can with forbearances and other issues. We have not seen a big jump up. Bundling doesn't occur. People generally have been putting pools of loans together and taking the whole pool and putting them into the marketplace.

Mr. SOUDER. Taking the other side of it, because part of my concern by schools and universities in the Higher Ed bill, one of my concerns was that by doing too rigid a standard on schools that were falling out, of having too many students default, if we didn't average that we were in fact going to dramatically impact low-income students, universities that reached out to a higher percentage of minorities, those in urban areas.

And I appreciate that the Chairman has worked with that. There, clearly the government may need to step in. But if we are going to just kind of average this, there is no incentive of the private sector or of the market to try to do any kind of responsible loan assessment. If all this stuff just gets bundled and averaged, the credit tightens up on everybody.

To me, where the government should be looking at stepping in is where we have high-risk cases. The people who have the least ability to pay can't maybe even make an adjustment for a technical school or others, and then the market can't meet it. And that is where the government comes in.

My concern in some of this discussion is that we are broad-brushing everybody, taking any accountability out of the universities, any accountability out of the individuals to adjust where they go, the number of years they go, the number of what decisions they make on career. And I was just a little concerned about the tone. I yield back.

Chairman MILLER. I thank the gentleman. And he raises a number of serious questions. And on top of that, of course, many of the States are sending the signal to their State institutions that they may have to raise fees or make cuts because State budgets are in trouble because of the same economic problems created by all the other actions in the credit market and in the economy.

Thank you very much for your time and your expertise this morning. I think you will probably be hearing from us. But more importantly, I hope you hear from the Secretary. I am I little dismayed at the end of this hearing, after this panel. You are out there a consumers of these services and as agents for the retail consumers of these services, and the fact that you have not had access to more concrete and better information is distressing. And it really does start to raise concerns.

I sent the Secretary a letter 2 weeks ago, but after listening to this, I just wonder whether or not they have a sense of urgency. Urgency and panic are two different things. Urgency about creating the standby system so that families and students will be able to continue to have access to this education on a timely basis I think should be a prime concern right now within the Department of Education.

As I said at the outset of the hearing, a course delayed, a semester delayed, or a quarter delayed can mean even greater financial hardships for these students and for these families. And that is what we seek to avoid.

I hope the markets correct. I hope there is a market answer. But we do have these two provisions on the books that at least we ought to run all of the traps, make them operational, make sure everybody understands them and has the options and they can make their choices. And hopefully that will work.

You will be hearing some more from us. Thank you very much for all of your time. Thank you to all the members of the committee for their attendance and their questions.

And I want to insert a statement into the record. Mr. Petri has asked to have a statement put in the record. And without objection, so ordered.

[The statement of Mr. Petri follows:]

**Prepared Statement of Hon. Thomas E. Petri, a Representative in Congress From the State of Wisconsin**

I want to thank Chairman Miller and Ranking Member McKeon for holding this important hearing today. I hope that after today's hearing students and parents will be confident that anyone who qualifies for federal students loans will be able to get them.

Numerous stories have been popping up in newspapers and other media warning that the current turmoil in the financial markets, fueled by subprime mortgages and the resulting credit crunch, will affect the availability of student loans. Most of these stories have failed to make the distinction between private and federal student loans.

The majority of students finance their education through federal loans. By law, students get those loans without credit checks and at virtually zero risk to the lenders because the government reimburses the lenders for any loan defaults. Currently, there are over two thousand lenders participating in the Federal Family Education Loan (FFEL) program. Should serious disruptions develop in the FFEL, by law the Department of Education is required to take up the slack.

Furthermore, students can get federal loans directly from the government through the Direct Loan Program. I look forward to hearing from the Education Department on the measures it has taken to ensure that the Direct Loan Program is prepared to take on any increase in loan volume.

In the mid-1990s, one third of the federal student loan market transitioned to the Direct Loan Program through a smooth operation created by the Department.

One would expect that after nearly fifteen years and improved technology the Direct Loan program could rapidly and smoothly expand from its present market share of 20%.

In fact, the Direct Loan Program is now delivered through the Common Origination and Disbursement System (COD) which is the same system that successfully delivers Pell Grants. Thus, any school which participates in the Pell Grant program should be able to easily switch to the Direct Loan Program.

Congress has a responsibility to ensure students' access to federal aid—and there are measures in place to do so. It is important today that we make sure that those measures are working properly.

Thank you, and I look forward to an informative hearing today.

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[Questions to witnesses from Mr. Scott follow:]

**Questions for the Record Sent to Witnesses Bauder, Johnson, Muilenburg, Sanders, and Wozniak**

Thank you for testifying at the March 14, 2008 hearing of the Committee on Education and Labor on "Ensuring the Availability of Federal Student Loans."

Representative Robert C. Scott (D-VA), a member of the Early Childhood, Elementary and Secondary Education Subcommittee and the Higher Education, Lifelong Learning and Competitiveness Subcommittee, has asked that you respond in writing to the following questions:

1. On the issue of income-contingent repayment, how many students participate? What is the cost, and who pays the cost, of writing off the remaining balance of those loans?

2. Is there any evidence that students purposefully select courses of study that lead to professions for which student loan write-offs may be available?

3. If we increased the amount of money available for student loans, how would the cost of these additional loans be scored for the purpose of "PAY-GO"?

4. How much of the cohort default rate is a function of credit worthiness of students (and their parents) before they attend school, as opposed to the effort the school makes to obtain repayment? Is there a better measure of the school's effort to obtain repayment than the cohort default rate? Does the cohort default rate unfairly punish those schools that admit low income and first generation students?

5. Testimony before the committee suggests that the major advantage to schools of the FFELP over the Direct Loan program is the fact that under FFELP, the private lender, not the school, shoulders the administrative expenses. The private lenders get a subsidy; would the schools be willing to take on the administrative expenses, if they received a smaller subsidy than the one we are now paying to the private lenders?

6. What would be the problems with treating student loans like mortgages in terms of going back and forth between fixed rates and variable rates at the discretion of the borrower depending on the interest rate conditions at the time?

7. What has the historical mix been between Pell grants, student loans and work-study? Are we providing enough assistance in the form of grants and work opportunities?

Please send an electronic version of your written response to the questions to the Committee staff by close of business on Friday, March 28, 2008—the date on which

the hearing record will close. If you have any questions, please do not hesitate to contact the Committee.

Sincerely,

GEORGE MILLER,
*Chairman.*

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[Responses to questions from witnesses follow:]

IOWA STATE UNIVERSITY,
*March 28, 2008.*

Hon. GEORGE MILLER, *Chairman,*
*Committee on Education and Labor, U.S. House of Representatives, Washington, DC.*

DEAR CHAIRMAN MILLER: In response to your inquiry of March 25, 2008, I offer the following:

1. On the issue of income-contingent repayment, how many students participate? What is the cost, and who pays the cost, of writing off the remaining balance of those loans?

The answer to this question is best directed to the U.S. Department of Education. It is my understanding that the taxpayer cost of cancellations is incorporated into the cost of each annual cohort of loans by both OMB and CBO. Those entities would best be able to answer the question about taxpayer costs.

From the standpoint of a student aid director and the students I represent, the income-contingent repayment (ICR) plan is an invaluable tool to support graduates who choose rewarding, but low-paying, employment. Also, in difficult economic times similar to those we are now seeing, the ICR plan provides families with a lifeline to avoid default. Because students can change repayment plans as frequently as necessary in the Federal Direct Loan Program, students can move into ICR to avert a default and return to a standard, graduated, or extended repayment plan when financial stability is regained.

2. Is there any evidence that students purposefully select courses of study that lead to professions for which student loan write-offs may be available?

I am not aware of any evidence to this effect. However, many aid directors work closely with faculty advisors and colleges/departments that are more likely to have students heading toward these careers. As an example, my staff work closely with our education department to make students aware of loan forgiveness options should they ultimately teach in an area that qualifies. Because there are narrow service requirements in the loan forgiveness programs, particularly in the out years, it can be difficult for students to take advantage of loan forgiveness options. For instance, an individual who qualifies for teacher loan forgiveness in the early years may find within several years that the employing school no longer qualifies as a high need area and loan forgiveness is no longer available.

3. If we increased the amount of money available for student loans, how would the cost of these additional loans be scored for the purpose of "PAY-GO"?

The additional cost related to increased loan limits would be affected by such things as whether the loans were subsidized or unsubsidized. As I understand the process, the Congress would determine any required "PAY-GO" offsets.

That being said, the amount of borrowing that is occurring within the private loan arena is a direct result of limits on federal student loans. Unfortunately for many undergraduates, their parents cannot (due to credit reasons) or will not seek funding through the PLUS loan program. These students have no other option except to borrow through a private loan. While the first recommendation would be for these undergraduate students to have higher loan limits available to them through the Stafford Loan program, if appropriate offsets are not available to make this feasible, expansion of the unsubsidized loan program to allow undergraduate students to borrow the cost of attendance less other financial aid (and available only via completion of the Free Application for Federal Student Aid) is an idea worth exploring. As a point of reference, with the introduction of the Graduate PLUS program in 2006, private loan borrowing by graduate students at my institution is now zero.

4. How much of the cohort default rate is a function of credit worthiness of students (and their parents) before they attend school, as opposed to the effort the school makes to obtain repayment? Is there a better measure of the school's effort to obtain repayment than the cohort default rate? Does the cohort default rate unfairly punish those schools that admit low income and first generation students?

Unlike the Federal Perkins Loan program, Federal Direct Loans are serviced by Department of Education contractors. At my institution, we take advantage of an option within the Direct Loan program called Late-Stage Delinquency reports. This allows my staff to make contact with students at various stages of delinquency to

remind them of their loan obligation and to assist them in seeking deferment/forbearance/repayment options that might help avert a default. We find that students are very receptive to working with us because we built a relationship with them during their tenure at our institution.

In my opinion, the creditworthiness of the student upon entering school is less a factor in default as is program completion and job opportunities after leaving school. I am concerned that because of the use of the cohort rate, some schools may choose not to participate in the federal loan programs, leaving their students no options but to borrow through more expensive private loans.

5. Testimony before the committee suggests that the major advantage to schools of the FFELP over the Direct Loan program is the fact that under FFELP, the private lender, not the school, shoulders the administrative expenses. The private lenders get a subsidy; would the schools be willing to take on the administrative expenses, if they received a smaller subsidy than the one we are now paying to the private lender?

That testimony, in my opinion, is not correct. Schools in both programs have some administrative expense such as certifying loan amounts, evaluating the place of loans in the entire aid package, and assisting students with speedy access to loan funds. These functions are the same in both programs. The additional expense for operating the direct loan program is minimal. Except for the addition of a promissory note, schools that administer Federal Pell Grants, the Academic Competitiveness Grant, National SMART Grant, and the impending TEACH Grant are already doing most of the things necessary to administer direct loans. The notion that Direct Lending is more difficult to administer than FFELP is a myth. In fact, I would argue that Direct Lending is significantly simpler because the aid officer, student, and parents always know exactly where to go to resolve loan issues—there is only one lender rather than the multiple players of lender, guarantor, and service agency that exist in FFELP. The simplicity of the Direct Loan program frees me and my staff to spend additional time with students counseling them on aid, assisting them in locating scholarship sources, help with debt management skills, and identifying other resources in the event of a detrimental financial event in the student's family.

6. What would be the problems with treating student loans like mortgages in terms of going back and forth between fixed rates and variable rates at the discretion of the borrower depending on the interest rate conditions at the time?

I believe that student borrowers should have as much flexibility as possible to refinance their loans at the best rates and terms available to them. The current structure does not support the best interests of students.

7. What has the historical mix been between Pell grants, student loans, and work-study? Are we providing enough assistance in the form of grants and work opportunities?

In the early 1980's when I began my career in financial aid, 75% of the typical student aid package was in the form of grant aid and family contribution. Today, the maximum Federal Pell Grant covers only 25% of the total cost of attendance at Iowa State University. Today, students at my institution are encumbered with debt—72.6% of the undergraduates borrowed to help meet their costs and the average debt upon graduation is $30,475 (which includes private loan borrowing).

As a result of stagnant or falling federal support, Iowa State University and many other institutions, have committed increasing gift aid to students. Some of these dollars are available as a result of fund-raising efforts while others are apportioned from tuition dollars collected from all students.

Work-study is a key funding source for students that often assist them in the out-of-pocket costs of college such as books, supplies, travel, etc. Work-study allocations have been flat for nearly a decade. This next year will be a particularly hard year to stretch these critical work-study dollars—while we support the increase in minimum wage for all workers, funds are exhausted more quickly as student are earning more. Also, due to the weakened economy, students who previously worked off-campus are returning to look for employment opportunities on-campus either because the cost of commuting to an off-campus job is prohibitive or because the community job market has tightened.

Thank you for the opportunity to provide follow-up to the hearing. If you or any other members of the committee have further questions, please contact me.

Sincerely,

ROBERTA JOHNSON,
*Director.*

**Answers for the Record Submitted by Ms. Muilenburg**

1. On the issue of income-contingent repayment, how many students participate? What is the cost, and who pays the cost, of writing off the remaining balance of those loans?

As a guarantor in the Federal Family Education Loan Program, USA Funds does not have recent, first-hand information about participation in the Income Contingent Repayment Program, which is only available under the Federal Direct Loan Program. Looking back at FY 2004 (the latest year for which the Education Department's budget appendix included this information), it appears that few borrowers with unconsolidated loans appear to be using the program. For example, for FY 2004, ED projected that only 3.2 percent of FDLP Stafford loan borrowers would opt for ICRP. In contrast, 45 percent of Direct Loan consolidation borrowers were expected to repay via income contingent repayment. For more recent data on the ICR program, I suggest you contact the Department of Education.

If a loan made under the ICR program is ultimately forgiven, there would be a cost to the federal government, and the amount forgiven is a tax liability for the student loan borrower. Since ICRP loans can only be written off after 25 years and the program has not yet been in effect for 25 years, we do not know the actual federal cost of the write-off provision.

2. Is there any evidence that students purposefully select courses of study that lead to professions for which student loan write-offs maybe available?

We do not have data on the fields of study of student loan borrowers, and are not aware of any research that confirms the notion that borrowers pursue particular fields of study in order to take advantage of loan forgiveness options. It is too early to assess whether the new loan public service loan forgiveness provisions of the College Cost Reduction and Access Act, which will not take effect until 2009, will have such an impact.

3. If we increased the amount of money available for student loans, how would the cost of these additional loans be scored for the purpose of "PAY-GO"?

There are federal costs associated with increasing loan limits, and because the FFEL and FDL programs are entitlements, costs associated with increasing loan limits would be subject to "PAY-GO". However, increasing Unsubsidized Stafford loan limits would not appear to result in federal costs, according to the OMB Budget for fiscal year 2009. While USA Funds strongly believes increasing federal loan limits is appropriate in order to reduce reliance on more expensive private loans, the current challenges FFELP lenders are facing in the capital markets will not be resolved by increasing loan limits.

4. How much of the cohort default rate is a function of credit worthiness of students (and their parents) before they attend school, as opposed to the effort the school makes to obtain repayment? Is there a better measure of the school's effort to obtain repayment than the cohort default rate? Does the cohort default rate unfairly punish those schools that admit low income and first generation students?

Federal Stafford loans are available to students without regard to credit worthiness, and parent PLUS loans are not counted in an institution's cohort default rate. Schools participating in the federal student loan programs are not formally charged with ensuring that their former students repay their loan obligations, but rather to perform entrance and exit counseling to ensure students understand their rights and responsibilities. Guarantors such as USA Funds, also work closely with student loan borrowers to avert defaults, and assist schools with debt management services they can use to contact their former students to help in the default prevention effort.

With respect to schools' cohort default rates, the cohort default rate is an imperfect measure of a school's educational quality. Schools that do admit significant percentages of low-income, first-generation students can be unfairly stigmatized by the use of the default rate as a proxy for the quality of instruction as well as continued participation in the Title IV program. The reasons for the higher default rates at these schools are several including: (1) low income students tend to be at higher risk; (2) higher risk students tend not to graduate on the same time schedule as students not in that category; (3) higher drop out rates are strongly correlated to higher default rates; and (4) adverse economic conditions/increased unemployment rates lead to increased inability to repay student loans, which disproportionately affect low income students and the institutions they attend.

The factor most closely linked to student loan defaults is the borrower's failure to complete his or her academic program. Dropouts are at much higher risk for loan default because, even though they may have less college debt than graduates, they lack the diploma necessary to obtain the better paying positions that graduates re-

ceive. Therefore initatives the promote student retention and completion also contribute to lower loan default rates.

5. Testimony before the committee suggests that the major advantage to schools of the FFELP over the Direct Loan program is the fact that under FFELP, the private lender, not the school, shoulders the administrative expenses. The private lenders get a subsidy; would the schools be willing to take on the administrative expenses, if they received a smaller subsidy than the one we are now paying to the private lenders?

As a student loan guarantor in the FFELP, and not an educational institution, USA Funds cannot speak to the issue of whether schools would prefer to participate in the Direct Loan program if they were provided administrative fees. I would note, however, that many of the services we provide, such as financial literacy materials and training, as well as customized debt-management services that institutions can use to work with their former students to help prevent defaults—all of which are provided free of charge—are simply not available to schools under the Direct Loan program.

6. What would be the problems with treating student loans like mortgages in terms of going back and forth between fixed rates and variable rates at the discretion of the borrower depending on the interest rate conditions at the time?

Federal student loans are subsidized and backed by the federal government, with no fees paid by borrowers who choose, for example, to consolidate their loans. This is in contrast to home mortgages, where homeowners who choose to refinance their mortgages to get a better interest rate or loan terms, generally pay significant fees in order to do so. In addition, the terms of a promissory note signed by a borrower contain the specific terms of the loan, including the interest rate, so it would not be possible to simply switch from a fixed to a variable rate loan and vice versa without a new promissory note. Finally, the cost of the federal student loan subsidies under such a scenario could increase dramatically.

7. What has the historical mix been between Pell grants, student loans and work-study? Are we providing enough assistance in the form of grants and work opportunities?

According to the College Board's "Trends in Student Aid 2007", federal grant aid to undergraduate and graduate students increased 83 percent in inflation-adjusted dollars over the past decade, and federal student loans increased by 61 percent over the same time period. Today, nearly $86 billion in federal grant aid is provided to undergraduate and graduate students, compared with $38 billion a decade earlier.

However, because of increases in the cost of postsecondary education, growth of enrollments in higher education over time, and changes in the structure of aid programs, these increases do not necessarily make college more affordable for individual students. For instance, the economic impact of Pell Grants has diminished considerably over the past 20 years. In 1987-88, the $2,100 maximum Pell Grant, covered 50 percent of tuition and fees and room and board charges at the average four-year public college or university and 20 percent of average total charges at private four-year institutions. However, in 2007-08, the $4,310 maximum Pell Grant equals only 32 percent of the average total charges at public colleges and universities and 13 percent for private, four-year institutions.

Moreover, federal work-study funds and other campus based aid continue to account for only a small percentage of all student aid, about 1 percent. A total of $776 million was provided for work-study a decade ago, compared with nearly $1.2 billion today, an increase of only 18 percent.

As a result, students are increasingly turning to loans to help finance their higher education. In the 1996-97 academic year, the average amount borrowed under the Stafford and PLUS programs for undergraduate students was $8,069, compared with $11,179 today (a 39 percent increase).

Clearly, federal student loans are and will remain a vital component of federal financial aid. However, USA Funds strongly supports increasing need-based grant aid to ensure that a postsecondary education continues to be an attainable goal for all American families.

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March 28, 2008

<u>VIA ELECTRONIC MAIL</u>
The Honorable George Miller
Chairman
House Committee on Education & Labor
B346 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Miller,

Thank you for the opportunity to provide feedback on this most important issue of ensuring the availability of Federal student loans.

Please see the answers provided below in response to your questions presented on Representative Scott's behalf:

1. **On the issue of income-contingent repayment, how many students participate? What is the cost, and who pays the cost, of writing off the remaining balance of those loans?**

   As I am sure you are aware, this repayment option is only available to students that have loans through the Direct Loan program and not for FFELP borrowers, therefore, I must defer to the Department of Education to provide these answers.

2. **Is there any evidence that students purposefully select courses of study that lead to professions for which student loan write-offs may be available?**

   South Carolina does have several programs such as the Teachers Loan program that we operate for the state which provides forgiveness of a borrowers' loan balance upon meeting select criteria, such as teaching in critical geographic or subject areas. There is compelling evidence to show that students do enter the teaching profession in order to qualify to have their loans forgiven. We have had approximately 20,000 residents in this program and of those nearly 86% have actually entered into the teaching profession.

3. **If we increased the amount of money available for student loans, how would the cost of these additional loans be scored for the purpose of "PAY-GO"?**

SC Student Loan has always been and will continue to be supportive of any additional funds that can be directed toward assisting students in achieving their higher education goals, whether those funds are made available through grants, scholarships, or loans. Increases were recently made to the Pell grant; however, these increases came at the expense of cuts to the student loan industry, not in the form of additional federal funding above the current level. As you are aware, the HERA and CCRAA acts combined to cut the FFEL program by approximately $40 billion. I cannot comment on how additional loans may be scored for the purpose of "PAY-GO".

4. **How much of the cohort default rate is a function of credit worthiness of students (and their parents) before they attend school, as opposed to the effort the school makes to obtain repayment? Is there a better measure of the school's effort to obtain repayment than the cohort default rate? Does the cohort default rate unfairly punish those schools that admit low income and first generation students?**

The cohort default rate has historically been the constant measure of repayment of student loans for comparison purposes. I believe the cohort default rate is a combination of several factors which include: 1) the credit-worthiness of the student and/or parent, 2) the preparedness of the student when entering the post-secondary institution, 3) whether or not the student completes their course of study, 4) the school's and the lender's efforts at educating the student borrower about responsible borrowing, and 5) the school's and lender's efforts at successfully resolving issues that may impede the repayment of the loan. In this sense, the cohort default rate may impact a school that admits a majority of low income or first generation students. I do believe that changing from a borrower-based cohort rate to a dollar-based cohort rate would be a more accurate measure of the true costs of defaults and would provide a fair basis for comparison among many schools with various socioeconomic and demographic compositions.

5. **Testimony before the committee suggests that the major advantage to schools of the FFELP over the Direct Loan program is the fact that under FFELP, the private lender, not the school, shoulders the administrative expenses. The private lenders get a subsidy; would the schools be willing to take on the administrative expenses, if they received a smaller subsidy than the one we are now paying to the private lenders?**

Although I cannot comment on behalf of the academic institutions in South Carolina, SC Student Loan as a FFELP lender does have an advantage over the Direct Loan program in that we are a state-based organization familiar with the needs of our students and families enabling us to provide local customer service. We also are able to achieve economies of scale in providing programs that meet the needs of students at all 55 of our educational institutions in South Carolina. In addition, we provide many programs for our middle and high schools throughout the state which are not served by the Direct Loan program. We also partner with

several organizations to offer benefits such as financial literacy programs, financial aid night presentations, and development of a comprehensive K-20 website, among many others, that individual institutions may not be in a position to offer even with a small subsidy provided. Finally, this program has proven successful at meeting the needs of students, families and schools for almost 40 years.

6. **What would be the problems with treating student loans like mortgages in terms of going back and forth between fixed rates and variable rates at the discretion of the borrower depending on the interest rate at the time?**

   The single most important detriment to treating student loans like mortgages in this sense is that lenders currently cannot pass on borrowing costs to the borrower as the end user due to the cap placed on the Special Allowance Payment, whereas mortgage lenders are able to pass on these costs. This would also lead to even greater confusion among borrowers. The risk incurred with the fluctuation of interest rates would also be borne by the government.

7. **What has been the historical mix between Pell grants, student loans, and work-study? Are we providing enough assistance in the form of grants and work opportunities?**

   I must defer to the Department of Education for this response as our organization does not have information pertaining to Pell grants or work-study programs.

Once again, I appreciate the opportunity to provide input on this issue and for the opportunity to address the committee at their hearing on March 14. SC Student Loan's mission as the state's non-profit lender is to provide programs of financial assistance to enable eligible students and parents to pursue and obtain their educational goals. We remain committed to that mission.

If I can be of further assistance, please do not hesitate to contact me at 803-612-5000.

Sincerely,

Charlie C. Sanders, Jr.
President & Chief Executive Officer

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MUNICIPAL SECURITIES GROUP,
UBS SECURITIES LLC,
*Purple Sage Park City, Utah, March 28, 2008.*

Hon. GEORGE MILLER, *Chairman,*
*Committee on Education and Labor, U.S. House of Representatives, Washington, DC.*

DEAR CHAIRMAN MILLER: Thank you for your follow up questions to my testimony of March 14, 2008. I would first like to remind the Committee that my expertise is primarily in the capital markets, asset-backed and municipal securities areas with a specialty in education loans. My background gives me access to reports and studies dealing with loan performance data, government cost scoring and other data solely regarding loan repayment. I have limited knowledge of the social implications of the loan programs on borrower decision making processes, the financial aid process with regard to grants or work study, or the manner in which individual schools

approach these issues with their matriculating students. With that stated here are my responses.

1. The income-contingent loan program is administered by the US Department of Education. They would be the party with access to data on the number of students enrolled and the cost of the program. As the income-contingent loan program is a program under the federal direct loan program, and the loan is an asset of the United States, the writing off of the remaining balance of these loans is a cost to the federal government.

2. This question is outside my area of expertise.

3. This question is also outside my area of expertise.

4. Federal Stafford loans do not permit credit assessments to be performed for the purpose of securing a loan. Hence, a comprehensive database may not be available to determine this. It is possible that studies of this nature may have been done that I am not aware. Sandy Baum of Skidmore College and a Senior Policy Analyst of the College Board may be someone who may be able to provide insight into these issues.

5. It is my understanding that schools have selected the FFELP program by a factor of 4 to 1 by dollar volume for a variety of reasons, not limited to administrative expenses. As my practice does not involve direct communications with school financial aid offices and their business officers, I cannot make an assessment as to the importance or willingness of schools to accept the additional administrative costs in return for remuneration.

6. The federal student loan program, both FFELP and Direct Loans, offer loans to students and parents at identical interest rates. Over the years, Congress has amended the Higher Education Act of 1965 on numerous occasions to change the interest rate or manner in calculation of the interest rate on student and parent loans. These changes in rate have a dramatic impact on the cost of the program to the federal government. When Congress increases rates to borrowers, the cost of the program to the federal government falls as it is the beneficiary of the higher rates in the Direct Loan Program and reduces the cost of subsidies to holders of loans in the FFELP program. Reducing rates to borrowers therefore, increases federal costs due to lower rates and higher subsidies.

Were the federal government to allow borrowers a choice of fixed or variable interest rates, the cost of such a program to the federal government would depend on the actual level of interest rates that occurred over the borrowing period. From a budget scoring perspective, this would depend on the assumptions used by CBO. CBO would also have to assume how many borrowers would select various options.

Because these loans are virtually always originated at below market interest rates, especially for unsecured, non-credit tested borrowers, it may be better for Congress to settle upon a single reasonable fixed interest rate that could remain in effect over long periods of time. This reduces the angst that might be created among borrowers over who got a better rate, or should I pick variable or fixed, and who is going to provide advice on such a decision which frankly is a subjective decision that the best minds in finance could not provide an absolute answer.

7. The College Board publishes a comprehensive study on this in its publication "Trends in Student Aid 2007". You may access it here:

*http://www.collegeboard.com/prod—downloads/about/news—info/trends/trends—aid—07.pdf*

The remainder of the question is beyond my area of expertise.

If you have any further questions, please do not hesitate to contact me.

Sincerely,

PAUL W. WOZNIAK.

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Chairman MILLER. And the committee will stand adjourned.

[Whereupon, at 12:45 p.m., the committee was adjourned.]