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LEGISLATIVE ANALYST'S OFFICE

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Overview of Student Loan Marketplace

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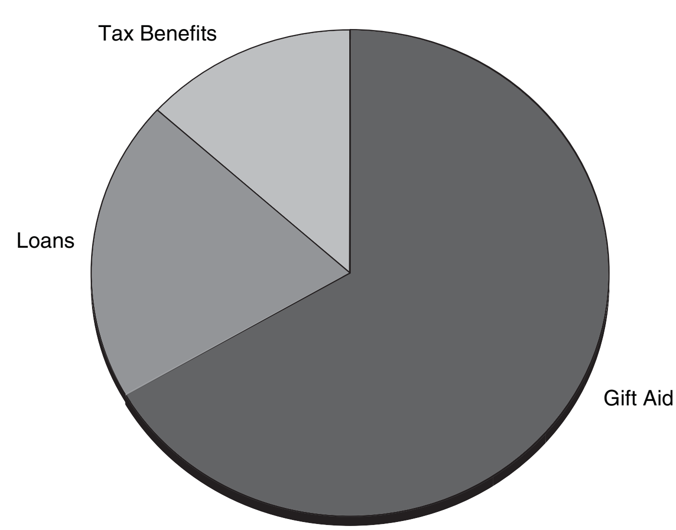
Presented to:
Senate Banking and Financial Institutions Committee
Hon. Bill Dodd, Chair

Purpose of Student Loans

Student Loans Are a Type of Financial Aid

- Financial aid helps students/families cover the costs of attending college. Aid can help cover tuition, books and supplies, and living expenses.
- Most financial aid is "need based"—that is, it aims to make college accessible for students/families who cannot afford to pay out of pocket.
- Main types of financial aid include:
  - Gift aid: grants, scholarships, and tuition waivers that students/families do not repay.
  - Tax benefits: reductions to income tax payments or tax refunds.
  - Loans: aid that students/families must repay over time.

Loans Comprise One Fifth of Financial Aid Received by Undergraduates Attending Public Colleges in California



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Types of Student Loans

Two Main Categories of Student Loans

- Federal student loans are made by the federal government.
- Nonfederal student loans are made by states, colleges, and financial institutions. Loans made by financial institutions are often referred to as "private" loans.
- Loan terms, including credit requirements, borrowing limits, interest rates, and loan fees, vary considerably.

Federal Student Loans

- The federal government currently has three student loan programs: (1) Direct Loans, (2) PLUS Loans, and (3) Perkins Loans.

Federal Government Has Three Student Loan Programs[a]

	Borrowers	Need Based?	Credit Requirement	Annual Limit[b]	Lifetime Limit[b]	Interest Rate[c]	Loan Fee	Grace Period
Direct Loans								
Subsidized	Undergraduates	Yes	None	$5,500	$23,000	3.8%	1.1%	6 months
Unsubsidized	Undergraduates	No	None	7,500[d]	31,000[d]	3.8	1.1	6 months
	Graduate students	No	None	20,500	138,500[e]	5.3	1.1	6 months
PLUS Loans	Graduate students	No	No adverse credit history	Up to cost of attendance	—	6.3	4.3	6 months
	Parents	No			—	6.3	4.3	—
Perkins Loans	Undergraduates	Yes	None	5,500	27,500	5.0	—	9 months
	Graduate students	Yes	None	8,000	60,000[e]	5.0	—	9 months

[a] Reflects current program rules for new loans.
[b] Amounts shown for undergraduates are for dependent students. Limits are higher for undergraduates who are independent.
[c] Fixed for the life of the loan. Congress sets the rate for Direct and PLUS loans based on market rates, plus a fixed amount. It has set a rate of 5 percent for Perkins loans. The federal government pays interest costs on subsidized Direct loans and Perkins loans while the student is in school.
[d] Including any amounts borrowed through subsidized loans.
[e] Including loans received for undergraduate study.

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Types of Student Loans *(Continued)*

☑ **Nonfederal Student Loans**

- **State Student Loans**
  - At least eight states (Alaska, Hawaii, Massachusetts, Minnesota, New Jersey, Texas, Washington, and Wisconsin) operate student loans programs.
  - Some state programs are limited to certain students, such as students demonstrating financial need or students in nursing and teaching programs.
  - Loan terms vary considerably across state programs. For instance, whereas Massachusetts' program charges no interest, Minnesota's program has a 6 percent fixed rate option and a 3.5 percent variable rate option.
- **College Student Loans**
  - Some public and private colleges operate their own student loan programs.
  - For example, some campuses at the University of California, California State University, and California Community Colleges operate student loan programs.
- **Private Student Loans**
  - Many banks, credit unions, and other financial institutions offer student loans.
  - Typically, private loans are capped at students' cost to attend college less other financial aid received.
  - Private lenders typically consider credit history and require a co-signer. They set interest rates depending on creditworthiness. Interest rates also tend to be variable.

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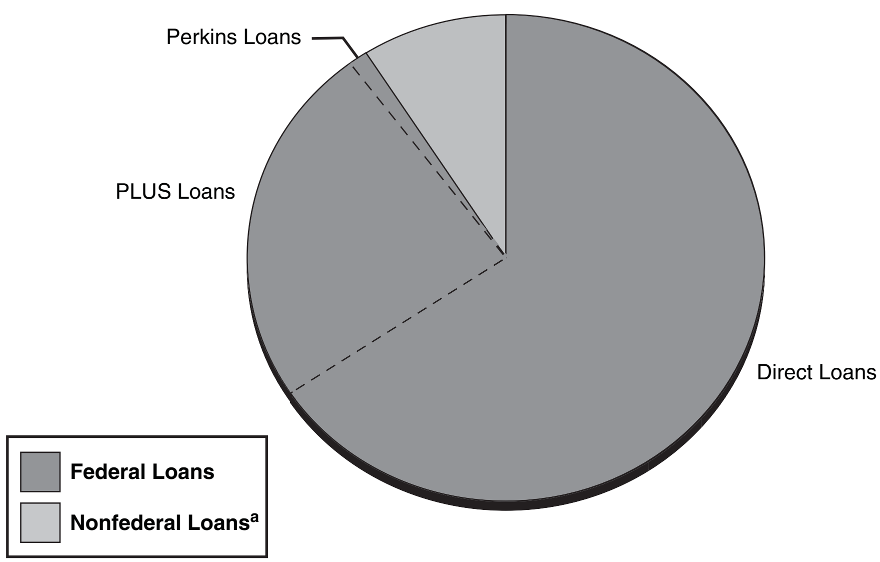
Student Loan Market

☑ **Federal Loans Make Up Vast Majority of Student Loan Market**

- In 2015-16, the federal government lent $8.3 billion to California students through its three loan programs.
- Precise data on nonfederal loan volume for California students is not available. However, various sources estimate nonfederal loans currently make up 8 percent to 10 percent of all student loans nationally. The figure below assumes nonfederal loans make up 9 percent of student loan borrowing for California students, or $830 million.

Federal Loans Make Up Vast Majority of California Student Loans



[a] Estimated based on national estimates of nonfederal student loan borrowing.

Student Loan Market *(Continued)*

☑ Federal Share of Student Loan Market Has Fluctuated Over Time

- Just prior to the start of the last recession in 2008-09, federal loans made up 75 percent of the national student loan market.
- At the height of the recession in 2010-11, the federal share of the national student loan market reached 94 percent. Primarily, this shift was due to private student lenders tightening student loan eligibility requirements.
- Since that time, the federal share has declined to about 90 percent of the national market.

☑ Students Attending Private Institutions Make Up Greater Share of Student Loan Market

- In California, about 25 percent of full-time equivalent enrollment is at private institutions (both nonprofit and for-profit), but about 65 percent of federal student loan dollars go to students attending these institutions.
- This is because students attending private institutions (1) are more likely to borrow and (2) borrow greater amounts, as compared to students attending public institutions.
- National-level data indicates students attending private institutions also make up a greater share of the private student loan market.

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Student Loan Servicers

☑ **Both Federal and Nonfederal Lenders Use Student Loan Servicers**

- Student loan servicers are organizations hired by lenders to "service" their loans. Servicers make loan disbursements, collect payments, and perform other administrative tasks.
- Both the federal government and many nonfederal lenders use student loan servicers.
- Four student loan servicers together service 94 percent of outstanding federal loan dollars.

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Student Loan Repayments

Federal Direct Loans Offer Traditional and Income-Based Repayment Plans

Seven Repayment Plans Available for Federal Direct Student Loans[a]

Plan	Monthly Payment	Repayment Period
Income-Driven Plans[b]		
Pay As You Earn	10 percent of discretionary income	Up to 20 years
Revised Pay As You Earn	10 percent of discretionary income	Up to 20 years
Income Based	10 percent of discretionary income[c]	Up to 20 years
Income Contingent	20 percent of discretionary income[d]	Up to 25 years
Traditional Plans		
Standard	Fixed	10 years
Graduated	Lower at first, then increases	10 years
Extended	Fixed or graduated	25 years

[a] Also applies to PLUS loans for graduate students but not parents.
[b] Payment must be less than payment under Standard plan to participate in Income Based and Pay As You Earn plans. For all plans, loan balances are forgiven at the end of repayment period. Discretionary income is the difference between a borrower's income and 150 percent of the poverty level (100 percent for the Income Contingent plan).
[c] For borrowers taking out their first federal loan after July 2014. Other borrowers pay 15 percent of discretionary income and have a 25-year repayment period.
[d] Payment also can be based on a 12-year repayment plan, adjusted for income.

- The federal government also operates a Public Service Loan Forgiveness Program for Direct Loan borrowers working in the public sector who make timely payments for the equivalent of ten years.

Nonfederal Repayment Plans Vary by Lender

- State and college lenders sometimes offer repayment plans similar to the federal government, though each lender establishes its own offerings.
- Private lenders typically do not offer income-based repayment plans, though some are starting to offer them.

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Student Loan Default Rates

Federal Loan Default Rates

- The federal government typically considers a loan to be in default if the borrower has not made a payment in more than 270 days.
- For Direct Loans and certain legacy federal loans, the federal government reports an average three-year cohort default rate of 10.4 percent for California institutions. This is slightly lower than the national average of 11.3 percent.

Private Loan Default Rates

- Private lenders typically consider a student loan to be in default if the borrower has not made a payment in 30 to 90 days.
- Data from the six largest private lenders indicates that 3 percent of loans currently are 30 to 90 days past due and an additional 2 percent are more than 90 days overdue.