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New Student Loan Legislation Halts Scheduled Rate Increase on Stafford Loans for One Year



On June 29, 2012, Congress approved legislation to stop the interest rate on federal subsidized Stafford Loans from jumping to 6.8% from 3.4% on July 1, 2012, for new college borrowers. The rate freeze is effective for one year.

Background

In 2007, Congress passed the College Cost Reduction and Access Act, which reduced the interest rates on subsidized Stafford Loans gradually over the next four academic years--from 6.8%, to 6.0%, to 5.6%, to 4.5%, and finally to 3.4%--with the provision that the rate would revert to 6.8% this July 1. With the nation's outstanding student loan debt topping \$1 trillion and the rise in college costs continually in the news, Congress came under pressure to halt the expiration of the 3.4% rate.

What does the new legislation do?

Under the new legislation:

- Rates on subsidized Stafford Loans will remain at 3.4% for undergraduates for one more school year--until July 1, 2013.
- As of July 1, 2013, undergraduate students with a subsidized Stafford Loan will have a maximum of six years of in-school status where the federal government will pay the interest on the loans while the student is in school. (Previously, the government paid the interest for as long as it took a student to get a diploma.)

The Congressional Budget Office has estimated that this one-year interest rate freeze will cost the federal government \$6 billion. It will be paid for primarily by reforms to the pension system.

What is a subsidized Stafford Loan exactly?

A Stafford Loan is a low-interest, federal loan made to undergraduate and graduate students who are attending college at least half-time. Stafford Loans come in two types--subsidized and unsubsidized.

With subsidized Stafford Loans, the federal government pays the interest that accrues on the loan while the student is in school, during any deferment periods, and for six months after graduation (hence the name "subsidized"). With unsubsidized Stafford Loans, students are responsible for paying the interest that accrues during the school year and deferment periods.

Subsidized Stafford Loans are the most popular federal education loan for student borrowers. Last year, the government estimates that approximately 7.5 million undergraduates and 1.8 million graduate students took out subsidized Stafford Loans. (As a reminder, as of July 1, 2012, graduate students will no longer be eligible for subsidized Stafford Loans.)

Subsidized Stafford Loans are based on financial need (as determined by the federal government's financial aid application, the FAFSA); unsubsidized Stafford Loans are not. The interest rate on unsubsidized Stafford Loans is fixed at 6.8% for new borrowers.



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