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Overhaul of Federal Student Loan Program

April 12, 2010

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- Pell Grants

- Income based repayment for federal student loans

With the nuances of health care reform getting all the attention, you may be surprised to learn that the recently passed health care legislation—the Patient Protection and Affordable Care Act of 2010, as amended by the Health Care and Education Reconciliation Act of 2010—includes several provisions related to college. The most noteworthy of these provisions involve:

- The distribution of federal student loans

The distribution of federal student loans

Currently, there are two ways to obtain a federal student loan—borrow directly from the federal government under the William D. Ford Federal Direct Loan (“Direct Loan”) program or borrow from a private lender who participates in the Federal Family Education Loan (FFEL) program. The FFEL program has been in existence since 1965 (the Direct Loan program since 1994), and private lenders in the FFEL program receive government subsidies to encourage them to loan money to students.

Under the new legislation, private lenders will no longer receive government subsidies to make federal student loans, and the FFEL program will be eliminated. Starting July 1, 2010, all federal student loans will be made directly from the federal government to borrowers under the Direct Loan program.

Generally, student borrowers shouldn't notice much of a difference with this change. If anything, the new system should be simpler and less confusing, because borrowers won't have to “shop around” for a private lender to obtain their federal student loans.

Parents who wish to take out a federal PLUS Loan might find themselves better off because the interest rate on a federal PLUS Loan obtained through the Direct Loan program is capped at 7.9%, compared to the interest rate on a federal PLUS Loan obtained through the FFEL program, which is capped at 8.5%.

Pell Grants

The Pell Grant is the federal government's largest financial aid grant program. It is available to undergraduate students with exceptional financial need (typically students from families who earn less than about \$45,000 per year). Graduate students aren't eligible.

The new legislation provides for automatic annual inflation-adjusted increases to the Pell Grant beginning in 2013. For the current academic year 2009/2010 (which runs from July 1, 2009, through June 30, 2010), the maximum Pell Grant is \$5,350. It is scheduled to increase to \$5,550 in 2010/2011, and will remain at that level for the following two years. It will then increase by the rate of inflation (via the consumer price index) in each of the next five years, reaching approximately \$5,900 in 2019/2020.

Income based repayment

On July 1, 2009, the federal government's new Income Based Repayment (IBR) program went into effect. The IBR program was created to help college graduates manage their increasingly large student loan payment obligations. Under the program, a borrower's monthly student loan payment is calculated based on income and family size. A borrower is allowed to pay 15% of his or her discretionary income to student loan payments, with any remaining debt forgiven after 25 years. The program is open to graduates with a federal Stafford Loan, Graduate PLUS Loan, or Consolidation Loan made under either the Direct Loan program or the FFEL program.

The new legislation enhances the IBR program. Under the legislation, borrowers who take out new federal student loans after July 1, 2014, will pay 10% of their discretionary income to student loan payments, with any remaining debt forgiven after 20 years.



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