STUDENT LOANS

HOW DID WE GET HERE?

GROWTH OF FEDERAL STUDENT LOANS

DOCUMENTARY FILM SERIES
Looking Back to Move Forward: A History of Federal Student Aid
In *A History of Federal Student Aid*, a documentary series produced by Lumina Foundation and the Institute for Higher Education Policy, key policy makers, their staff and education researchers provide insight into the evolution of federal student aid through their first-hand experiences with the policy making process. This short film on the history of federal student loans is one in a series of several that illuminates past seminal moments and offers instructive lessons and building blocks to guide newer policy innovations.
**HISTORICAL INFORMATION**


*Scene: 2:20 – 2:41 minutes*

The first federal loan program, the National Defense Student Loan (NDSL) Program, was created in 1958 by the National Defense Education Act (NDEA). Its emphasis was on improving education, science, mathematics, engineering, and foreign language programs during the Cold War in the aftermath of Sputnik.1 Funds for this loan program are given to campuses to distribute to students with financial need in the form of low-interest loans. Now called the Federal Perkins Loan Program and authorized through the Higher Education Act (HEA),2 the program no longer has a specific focus on certain fields, and is designed to be targeted to lower-income students on campus.

1965: Higher Education Act (HEA) – Guaranteed Student Loan (GSL) Program

*Scene: 2:41 – 4:55 minutes*

The next federal loan program was proposed in 1965 as a compromise with Congress: President Johnson wanted to create a national need-based scholarship, but Congress would approve the program only if a loan program for middle-income students was simultaneously created. Using an existing private program in Massachusetts as a model, the federal government created the Guaranteed Student Loan (GSL) Program, later renamed the Stafford Loan Program, through the 1965 HEA.3 The goal of GSL was to ease the burden of college costs for middle-income students by providing federally insured loans through private lenders.4

In the 1970s, federal loans quickly rose in volume due to the rise of college costs, creation of government-sponsored enterprises, establishment of state loan guarantee agencies, and expansion of loan eligibility and limits. Along the way, the government created several additional federally guaranteed loan programs. In 1992, these public–private programs became part of the newly created Federal Family Education Loan (FFEL) Program.5 FFEL had four components: Subsidized Stafford Loans, Unsubsidized Stafford Loans, Parent Loans for Undergraduate Students (PLUS) Program, and Federal Consolidation Loans. FFEL was eliminated in 2010, and student loans no longer originate under any of its programs.6

“We’ve seen an interesting evolution in terms of the student loan programs—from creating greater access to loans to ensuring that defaults don’t happen, to what we have now contemporarily, which is this interest in debt. But that really has been an evolution...”

**JAMIE MERISOTIS**
1972: HEA Reauthorization – Creation of Sallie Mae

Scene: 4:55 – 5:27 minutes

The Student Loan Marketing Association (Sallie Mae) was created through the 1972 HEA Reauthorization as a government-sponsored enterprise to increase liquidity and capital in the GSL Program by originating loans.\(^7\) In 1996, Congress passed the Student Loan Marketing Association Reorganization Act to restructure Sallie Mae as a private company. Although Sallie Mae had until 2008 to complete privatization, it took the company less than 10 years to become fully privatized.\(^8\) Sallie Mae stopped originating federal loans in 2010, when the federal government ended the FFEL Program and legislated that all loans be made directly from the government to students. Today, loans made from Sallie Mae and other lenders previously involved in the FFEL Program originate outside of federal subsidies and are thus considered private.

1978: Middle Income Student Assistance Act (MISAA) – Eliminated Income Requirement for Loans

Scene: 5:27 – 6:45 minutes

Under the original GSL Program terms, students with an adjusted family income of less than $15,000 would qualify for an interest-free loan while in college.\(^9\) However, in 1978, Congress eliminated any income requirement for borrowing under FFEL through the Middle Income Student Assistance Act (MISAA). The removal of this restriction allowed more students to be eligible,\(^10\) which caused an increase in program administration costs. This led to the creation of the student loan origination fee in 1981, allowing lenders to charge up to five percent of the loan in addition to the borrowed amount.\(^11, 12\) MISAA was repealed in 1981 through the Omnibus Budget Reconciliation Act, but the origination fee remained, with its proceeds, like all other proceeds, going to the federal government.\(^13\)

1980: HEA Reauthorization – PLUS Program

Scene: 6:45 – 7:25 minutes

To give students and their families more liquidity to pay for college, the PLUS Program was created for parents of dependent undergraduate students. Created in the 1980 HEA Reauthorization,\(^14\) loans in the PLUS Program were capped and offered at a higher interest rate than other federal loans. Just one year later, PLUS was extended to independent undergraduate students, along with graduate and professional students, and renamed the Auxiliary Loans to Assist Students (ALAS) Program.\(^15\) In 1986, however, ALAS was split into two parts: the Supplemental Loans to Students (SLS) Program, for graduate and independent students, and the Parent PLUS Program, specifically for parents of dependent undergraduate students (as the original PLUS Program had been intended). Both SLS and Parent PLUS had annual and aggregate borrowing limits.\(^16\) The 1992 HEA Reauthorization removed these limits for the Parent PLUS, but the cap for SLS remained.\(^17\) In 1993, the SLS Program was merged into the Unsubsidized Stafford Loan Program through the Student Loan Reform Act. Two years later, the Graduate and Professional Student PLUS (“Grad PLUS”) Program was created to provide further support for graduate and independent students.\(^18, 19\)

1986: HEA Reauthorization – Addressing Default Rates

Scene: 7:25 – 9:49 minutes

Concerns about default rates on student loans led Congress to implement, in the 1986 HEA Reauthorization, a number of policies meant to reduce these rates.\(^20\) The most noticeable change was that any student in default under the GSL Program could not receive new federal student assistance. The act also included provisions that prevented loan originators from falsely advertising to students and providing incentives to institutions to secure loan applicants. Additionally, it gave the U.S. Department of Education more regulatory and administrative power over student loan lenders. In 1990, Senator Sam Nunn (D-GA) held hearings to investigate high student loan default rates, especially at proprietary schools.\(^21\)
Bush Administration also expressed concerns about high levels of defaults on student loans. These efforts led to the establishment of the cohort default rate (CDR) in the 1990 Omnibus Budget Reconciliation Act, which eliminated student aid eligibility at schools with high default rates for three consecutive years. Originally, a school was no longer eligible if 35 percent or more of its students were in default, but this threshold has fluctuated over the years. In 1992, the U.S. Department of Education was authorized to determine the CDR threshold annually and mandated that CDRs be calculated using students who enter default within two years of entering repayment. The 1993 Higher Education Opportunity Act changed the way CDRs were calculated to include students who default within three years after they enter repayment and mandated that the U.S. Department of Education publish cohort default rates for each type of institution. Today, schools may lose eligibility to disperse federal student loans if their CDR is over 40 percent for any given year in the past three years or over 30 percent for three consecutive years. See figure 1 for the two-year national student loan default rates between 1987 and 2011.

1992: HEA Reauthorization – Direct Loan Program

In the early 1990s, the FFEL Program was becoming a large budgetary expense and posed management challenges. The idea emerged of a program in which the U.S. Department of Education would give loans directly to students. The Federal Direct Loan Program started in 1992 with the establishment of a demonstration program that called for 300 institutions to begin offering direct loans. The 1993 Omnibus Budget Reconciliation Act, which legislated the start of the Federal Direct Loan Program to be in 1994, required participating institutions to gradually give more Direct Loans each year. Starting in 2010, the FFEL Program was eliminated and all new federal loans since then—except for Perkins Loans—have been distributed directly to students from the U.S. Department of Education.
1992: HEA Reauthorization – Increase in Loan Limits/Unsubsidized Stafford Loans

Scene: 11:31 – 12:29 minutes

Since the GSL Program’s creation, annual and aggregate loan limits for students borrowing through it have increased. In the 1992 HEA Reauthorization, Congress significantly increased the annual GSL loan limits for students in their second, third, and fourth years by about 33 to 38 percent (see figure 2). For example, annual loan limits increased from $4,000 to $5,500 for students in their third and fourth year of school. Aggregate loan limits also increased by at least 20 percent (see figure 3). For undergraduate students specifically, aggregate loan limits increased from $17,250 to $23,000. Today, annual and aggregate loan limits are much higher than they were in 1992. Additionally, this 1992 reauthorization created the Unsubsidized Stafford Loan Program to make loans more readily available to middle-income students. These loans had the same rules as subsidized loans but without the interest subsidies during college.

1993: Student Loan Reform Act – Income-Contingent Repayment (ICR) Plan

Scene: 12:29 – 13:01 minutes

As limits on borrowing were increased and college costs were rising, many students were having trouble repaying loans through the standard repayment plan—fixed payments for 10 years based on the amount borrowed. To provide an alternative repayment plan specifically for Direct Loan borrowers with lower earnings, the Income-Contingent Repayment (ICR) Plan was introduced in 1993 through the Omnibus Budget Reconciliation Act, more commonly referred to as the Student Loan Reform Act. All loans under the Direct Loan Program except Parent PLUS, unless consolidated into a Direct Consolidation Loan, are eligible for repayment under the ICR Plan. Payments for the ICR Plan are either 20 percent of discretionary income or a 12-year fixed repayment plan—whichever is the lower of the two options. The remaining balance is forgiven after 25 years of payments.


FIGURE 3:
Stafford Aggregate Loan Limit Changes Due to the 1992 HEA Reauthorization

FIGURE 4:
Current Loan Limits

<table>
<thead>
<tr>
<th>Year</th>
<th>Dependent Students</th>
<th>Independent Students</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual Loan Limits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>First Year</td>
<td>$5,500 – Up to $3,500 in subsidized loans.</td>
<td>$9,500 – Up to $3,500 in subsidized loans.</td>
</tr>
<tr>
<td>Second Year</td>
<td>$6,500 – Up to $4,500 in subsidized loans.</td>
<td>$10,500 – Up to $4,500 in subsidized loans.</td>
</tr>
<tr>
<td>Third Year and Beyond</td>
<td>$7,500 – Up to $5,500 in subsidized loans.</td>
<td>$12,500 – Up to $5,500 in subsidized loans.</td>
</tr>
<tr>
<td>Graduate or Professional Students</td>
<td>Not Applicable – Graduate and professional students are considered independent.</td>
<td>$20,500 (unsubsidized only)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Subsidized and Unsubsidized Aggregate Loan Limit</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>$31,000 – Up to $23,000 in subsidized loans.</td>
<td>$57,500 for undergraduates – Up to $23,000 in subsidized loans.</td>
</tr>
<tr>
<td>$138,500 for graduate or professional students – Up to $65,500 in subsidized loans.</td>
<td>Includes loans received for undergraduate studies.</td>
</tr>
</tbody>
</table>

Source: U.S. Department of Education, Federal Student Aid, Subsidized and Unsubsidized Loans, Table: How Much Can I Borrow?

Note: Dependent students whose parents are unable to obtain PLUS must abide by the loan limits for independent students.
Today, seven student loan repayment plans exist—four based on income and three with fixed or graduated payments (see page 16 for additional information). Although three of these repayment plans were not mentioned in the video, they play an important role for many students. The Graduated and Extended Repayment plans were introduced in 1993 through the Omnibus Budget Reconciliation Act, along with the ICR Plan. Both were modeled after the Standard Plan, but the Graduated Plan allows students to repay their loans on a graduated scale, while the Extended Plan allows students up to 25 years to repay their loans with either fixed or graduated payments. The Income-Sensitive Repayment Plan was introduced in 1998 to provide a repayment plan similar to the ICR Plan for FFEL borrowers but with 10 years of repayment, instead of 25.0
# CURRENT FEDERAL STUDENT LOAN PROGRAMS

## KEY FACTS

<table>
<thead>
<tr>
<th>Perkins Loan Program</th>
<th>Direct Unsubsidized Loans</th>
<th>Direct Subsidized Loans</th>
<th>Direct PLUS Loans</th>
</tr>
</thead>
</table>

### Overview

The Federal Perkins Loan Program provides low-interest loans to low-income students. Borrowers usually repay loans directly to their educational institutions.

*Note: The Perkins Loan Program is set to expire in 2015.*

The Federal Direct Unsubsidized Loan Program provides loans directly from the U.S. Department of Education to students. Interest begins accruing upon borrowing.

The Federal Direct Subsidized Loan Program provides loans directly from the U.S. Department of Education to students with financial need. Interest is subsidized through college and a six-month grace period following degree completion, along with any deferment periods.

The Direct PLUS Program allows for parents of dependent undergraduate students to borrow supplemental loans to the students’ Direct Subsidized and Unsubsidized Loans. The PLUS Program is also available to graduate and independent students.

### Major Shifts

Since fiscal year 2005, no new federal funds have been contributed. Currently, funds generated from institutions’ loan collections and reimbursements from the U.S. Department of Education for loan cancellations are used to make new loans.

As of 2012, subsidized loans are no longer offered to graduate students.

### Interest Rate

<table>
<thead>
<tr>
<th></th>
<th>4.29% for undergraduate students</th>
<th>4.29% for undergraduate students</th>
<th>6.84% for parents and graduate or professional students</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perkins</td>
<td>5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsubsidized</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidized</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Origination Fee

<table>
<thead>
<tr>
<th></th>
<th>1.068%</th>
<th>1.068%</th>
<th>4.272%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perkins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsubsidized</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidized</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Number of Recipients

<table>
<thead>
<tr>
<th></th>
<th>501,615 undergraduate students (2012)</th>
<th>6.49 million undergraduate students</th>
<th>6.9 million undergraduate students</th>
<th>704,000 parents of undergraduate students</th>
<th>343,000 graduate students (Parent and Grad PLUS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perkins</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsubsidized</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidized</td>
<td></td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>

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*† For Loans Disbursed on or After July 2015*

*‡ For Loans First Disbursed Between October 2015 and 2016*
## CURRENT FEDERAL STUDENT LOAN REPAYMENT PLANS

### KEY FACTS

<table>
<thead>
<tr>
<th>Plan Type</th>
<th>Created</th>
<th>Payments</th>
<th>Repayment Period</th>
<th>Predetermined Forgiveness</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard Repayment Plan</td>
<td>1965</td>
<td>Fixed, at least $50 per month</td>
<td>Up to 10 years</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Graduated Repayment Plan</td>
<td>1993</td>
<td>Graduated (lower at first, then increases slowly)</td>
<td>Up to 10 years</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Extended Repayment Plan</td>
<td>1993</td>
<td>Fixed or graduated</td>
<td>Up to 25 years</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Income-Contingent Repayment (ICR)</td>
<td>1993</td>
<td>Either 20% of discretionary income or the amount paid on a 12-year fixed</td>
<td>Up to 25 years</td>
<td>N/A</td>
<td>After 25 years of qualified monthly payments for borrowers taking out loans prior to July 1, 2014.</td>
</tr>
<tr>
<td>Income-Sensitive Repayment (ISR)</td>
<td>1998</td>
<td>Based on annual income</td>
<td>Up to 10 years</td>
<td>N/A</td>
<td>After 20 years of qualified monthly payments for new borrowers as of July 1, 2014.</td>
</tr>
<tr>
<td>Income-Based Repayment (IBR)</td>
<td>2007</td>
<td>Up to 15% of discretionary income for borrowers taking out loans prior to July 1, 2014.</td>
<td>Up to 25 years</td>
<td>N/A</td>
<td>After 25 years of qualified monthly payments for borrowers taking out loans prior to July 1, 2014.</td>
</tr>
<tr>
<td>Pay As You Earn (PAYE)</td>
<td>2010</td>
<td>Generally 10% of discretionary income</td>
<td>Up to 20 years</td>
<td>N/A</td>
<td>After 20 years of qualified monthly payments for new borrowers as of July 1, 2014.</td>
</tr>
</tbody>
</table>

### NOTES

1. Unless otherwise noted, information was collected from each program’s corresponding webpage, found at https://studentaid.ed.gov/repay-loans/understand/plans.
2. Borrower must pay income tax on remaining loans if loans are forgiven after the predetermined time frame.
3. Borrowers must demonstrate financial hardship to qualify for IBR and PAYE.
Massachusetts Higher Education Assistance Corporation (MHEAC)
» Started a guaranteed student loan program in Massachusetts, which insured student bank loans with money raised through philanthropic donations from local businesses.54

National Defense Education Act (NDEA)
» Created the National Defense Student Loan (NDSL) Program, the first federal loan program, now called the Federal Perkins Loan Program.57 Distributed to students by institutions, these loans required a monetary match from institutions. Total amount students could borrow for any fiscal year was capped at $1,000, up to a total of $5,000 for all years. Annual and aggregate loan limits have fluctuated ever since.

Higher Education Act (HEA)
» Formed the Guaranteed Student Loan (GSL) Program, a public–private partnership to provide low- and middle-income students with money for college.58 Originally, undergraduate students could borrow no more than $1,000 per year, with an aggregate limit of $5,000. Graduate students could borrow no more than $1,500 per year, with an aggregate limit of $7,500. Since then, annual and aggregate loan limits have fluctuated.69 Loans were to be repaid in no more than 10 years in payments of no less than $360 per year or the remaining balance, with repayment periods to be decided between the lender and borrower.60 This was known as the Standard Repayment Plan.

HEA Reauthorization
» Allowed lenders to have student loans qualify for federal insurance if no such state or nonprofit insurance program existed to cover a student, which led to a private increase in lending in the GSL Program.61

1956
Massachusetts Higher Education Assistance Corporation (MHEAC)

1958
National Defense Education Act (NDEA)

1965
Higher Education Act (HEA)

1968
HEA Reauthorization

1972
HEA Reauthorization
» Created the Student Loan Marketing Association (Sallie Mae) in order to buy loans from lenders and provide lenders with more capital.62

1976
HEA Reauthorization
» Provided incentives for states to establish loan guaranty agencies, which insured federal student loans made by lenders.63

1978
Middle Income Student Assistance Act (MISAA)
» Eliminated the $15,000 income requirement for GSL, which allowed middle- and high-income students to qualify for loans.64

1980
HEA Reauthorization
» Created the Parent Loans for Undergraduate Students (PLUS) Program.65

1981
Omnibus Reconciliation Act
» Repealed MISAA.66
» Replaced the PLUS Program with the Auxiliary Loans to Assist Students (ALAS) and extended borrowing to graduate and independent undergraduate students.67
» Imposed borrower loan origination fee on new loans.68

1986
HEA Reauthorization
» Split ALAS into the Supplemental Loan to Students (SLS) for graduate and independent students, and PLUS for parents.69
» Added Consolidation Loans, but borrowers who had loans with different lenders could not consolidate (known as the single holder rule).70
» Introduced measures to decrease the student loan default rate including but not limited to giving the U.S. Department of Education more regulatory and administrative power over lenders,71, 72 restricting guaranty agencies from offering some incentives to educational institutions,73 and banning students in default from receiving federal student assistance.74
Omnibus Reconciliation Act
» Established the cohort default rate (CDR) to eliminate student aid eligibility at high default schools for repeated offenders over three consecutive years.75

HEA Reauthorization
» Introduced direct loans through a demonstration program.76
» Officially made Unsubsidized Stafford Loans available to students.77
» Created the Federal Family Education Loan (FFEL) Program, consisting of Stafford Loans and PLUS.78
» Assigned the U.S. Department of Education to determine and publish CDRs annually, and mandated that CDRs be calculated for students who default within two years of entering repayment.79
» Removed annual and aggregate borrowing limits on PLUS Loans.80

Omnibus Budget Reconciliation Act
(also known as the Student Loan Reform Act)
» Established the Income-Contingent Repayment (ICR) Plan, Extended Repayment Plan, and Graduated Repayment Plan for Direct Loan borrowers.81
» Formally called for a phasing-in of the Direct Loan Program to begin in 1994.82

Student Loan Marketing Association Reorganization Act
» Required Sallie Mae to reorganize itself as a private company and cease to exist as a government-sponsored entity.

HEA Reauthorization
» Established the Income-Sensitive Repayment (ISR) Plan, specifically for FFEL borrowers.83
» Allowed FFEL borrowers to be eligible for Extended and Graduated Plans.84

Higher Education Reconciliation Act (HERA)
» Allowed for graduate and professional students to borrow through the PLUS Program.85

Emergency Appropriations Act
» Single holder rule repealed, allowing borrowers to consolidate loans between lenders.86

College Cost Reduction and Access Act (CCRAA)
» Established the Income-Based Repayment (IBR) Plan.87

Higher Education Opportunity Act (HEOA)
» Mandated that CDRs be calculated to include students in default three years after entering repayment and that the U.S. Department of Education publish CDRs for each type of institution.88

Ensuring Continued Access to Student Loans Act (ECASLA)
» Temporarily authorized the U.S. Department of Education to buy loans from private lenders to ensure that students had access to loans during the financial market downturn.89

Health Care and Education Reconciliation Act (HCERA)
» Changed the IBR terms for borrowers taking out their first loans after July 1, 2014.90
» FFEL Program eliminated.91

Budget Control Act
» Eliminated subsidized loans for graduate and professional students.92

Executive Order
» Established the Pay As You Earn (PAYE) Plan with more generous repayment and forgiveness terms than available through IBR. Eligible borrowers were individuals who took out their first loans after September 2007 and were still borrowing after September 2011.93 This plan became available in 2012.

Executive Order
» Expanded the PAYE Plan to individuals who borrowed after September 2007 but stopped borrowing by September 2011. This plan is not yet currently available.94
FEATURED EXPERTS

Pauline Abernathy  

Melody Barnes  
Director, White House Domestic Policy Council, 2009–2012

Sandy Baum  
Independent Consultant, College Board, 2004–2013

David Bergeron  

John Dean  

David Evans  

Sarah Flanagan  

Richard Jerue  

David Longanecker  
Assistant Secretary for Postsecondary Education, U.S. Department of Education, 1993–1999

Daniel Madzelan  

Jamie Merisotis  
Executive Director, National Commission on Responsibilities for Financing Postsecondary Education, 1991–1993

Barmak Nassirian  

Thomas Parker  
Co-Founder and President, The Education Resources Institute, 1981–2001

Kenneth Redd  

Joseph Russo  
Director of Student Financial Aid, Notre Dame University, 1978–2012

Robert Shireman  

Margaret Spellings  

Tom Wolanin  
45 Ibid.
Lumina Foundation is an independent, private foundation committed to increasing the proportion of Americans with high-quality degrees, certificates and other credentials to 60 percent by 2025. Lumina’s outcomes-based approach focuses on helping to design and build an accessible, responsive and accountable higher education system while fostering a national sense of urgency for action to achieve Goal 2025.

The Institute for Higher Education Policy (IHEP) is a nonpartisan, nonprofit organization committed to promoting access to and success in higher education for all students. Based in Washington, D.C., IHEP develops innovative policy- and practice-oriented research to guide policymakers and education leaders, who develop high-impact policies that will address our nation’s most pressing education challenges.