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CONSOLIDATION LOANS: WHAT'S BEST FOR PAST BORROWERS, FUTURE STUDENTS, & U.S. TAXPAYERS?

HEARING

BEFORE THE

SUBCOMMITTEE ON 21ST CENTURY COMPETITIVENESS

OF THE

COMMITTEE ON EDUCATION AND THE WORKFORCE
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

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CONSOLIDATION LOANS: WHAT'S BEST FOR PAST BORROWERS, FUTURE STUDENTS, & U.S. TAXPAYERS?

Tuesday, July 22, 2003
U.S. House of Representatives
Subcommittee on 21st Century Competitiveness
Committee on Education and the Workforce
Washington, DC

The Subcommittee met, pursuant to notice, at 10 a.m., in room 2175, Rayburn Office Building, Hon. Howard P. "Buck" McKeon [Chairman of the Subcommittee], presiding.

Present: Representatives McKeon, Isakson, Petri, Johnson, Ehlers, Osborne, Carter, Burns, Kildee, Tierney, Kind, Wu, Holt, McCarthy, Van Hollen, Ryan, and Hinojosa.

Ex Officio present: Representative Boehner.

Also present: Representatives Bishop and Hoekstra.

Staff present: Kevin Frank, Professional Staff Member; Cindy Herrle, Senior Budget Analyst; Alexa Marrero, Press Secretary; Susan Oglinsky, Coalitions Advisor; Alison Ream, Professional Staff Member; Deborah L. Samantar, Committee Clerk/Intern Coordinator; Dave Schnittger, Communications Director; Kathleen Smith, Professional Staff Member; Holli Traud, Legislative Assistant; Ellynne Bannon, Minority Legislative Associate/Education; Ricardo Martinez, Minority Legislative Associate/Education; Alex Nock, Minority Legislative Associate/Education; and Joe Novotny, Minority Legislative Assistant/Education.

Chairman McKEON. A quorum being present, the Subcommittee on 21st Century Competitiveness will come to order.

We're meeting today to hear testimony on consolidation loans: what's best for past borrowers, future students and U.S. taxpayers. Under Committee Rule 12, the opening statements are limited to the Chairman and Ranking Minority Member of the Subcommittee; therefore, if other members have statements, they may be included in the hearing record.

With that, I ask unanimous consent for the hearing record to remain open 14 days to allow member statements and other extraneous material referenced during the hearing to be submitted in the official hearing record.

Without objection, so ordered.

I now read my opening statement.

STATEMENT OF HON. HOWARD P. "BUCK" McKEON, CHAIRMAN, SUBCOMMITTEE ON 21st CENTURY COMPETITIVENESS

Good morning. I want to thank all of you for joining us for this important hearing on the consolidation loan program. As we move forward with our efforts to reauthorize the Higher Education Act, we continue to address the many issues within that Act in order to help make post-secondary education a reality for low income students who previously had little chance of pursuing such a dream. This hearing is another in our continuing series and is meant to provide information to the members of this Committee about one of the loan programs within the Higher Education Act.

Earlier today, Chairman Boehner and I joined together to unveil the principles that will guide the remainder of the reauthorization of the Higher Education Act. When the Higher Education Act was authorized in 1965, its intention was to expand access and provide opportunities to low income students. Yet, today I believe some of the higher education programs have lost sight of that original mission and the crisis of skyrocketing college costs makes it more important than ever to ensure the higher education programs are reaching their full potential to expand access to higher education in America.

I believe the principles we have outlined will help us address this crisis and realign programs under the Higher Education Act to more fully meet the goal of expanding access to a college education. Briefly, these principles are: holding colleges accountable for cost increases, removing barriers, particularly those that disproportionately harm non-traditional students, improving quality and innovation by empowering consumers, and realigning student aid programs to ensure fairness for America's neediest students and families. These principles will guide reforms to all areas in the Higher Education Act, including the Consolidation Loan Program, which is the topic of today's hearing.

The Consolidation Loan Program was implemented as part of the reauthorization of the Higher Education Act in 1986. The intent of the Consolidation Loan Program was to provide an opportunity for borrowers with multiple loan holders and a high level of student loan debt to consolidate that debt with one holder to allow for 1 monthly payment. The program often provides a longer repayment period as well, thereby lowering the borrower's monthly payment.

When a borrower applies for and receives a consolidation loan, all underlying loans are paid in full by the consolidating lender and a new loan is created in the amount of the debt paid in full. The repayment term for that loan is then determined by the borrower's outstanding debt at a fixed interest rate up to a maximum of 30 years.

When the program was originally developed, it was done so as a way to address a specific issue - providing for an opportunity to consolidate debt with one holder. While the interest rate structure for this program has changed over time, it has always called for a somewhat higher rate than the underlying loans. It is only because of the recent low variable rate, which was a result of our reauthorization in '98, that we worked so hard on, the rates for this program has now taken on a mantle of a home mortgage, even though it is totally dissimilar.

With this rate decline, the program has seen a dramatic increase in the number of borrowers choosing to consolidate. In 1998, there were 160,000 FFELP consolidation borrowers and 106,000 direct loan consolidation borrowers. In 2002, there were 717,000 FFELP consolidation borrowers and 363,000 direct consolidation borrowers.

In terms of loan volume, there has been an almost 600 percent increase in FFELP volume and an approximately 270 percent increase in direct loan volume in the consolidation loan program. While some of that increased volume is due to the availability of lower interest rates, some may be due to the increase in the number of organizations specifically marketing consolidation loans, which had not occurred in years past.

There is no question that I and my colleague, Mr. Kildee, support the availability of low, variable interest rates for students. As you know, the changes we made in the last reauthorization put in place the same variable rate formulas that have provided for the lowest rates in the loan program's history.

With the ever-rising costs of post-secondary education in this country, we want to continue to do all that we can to increase affordability and access to post-secondary education for low and moderate income students. However, I believe achieving that goal will require us to look carefully at where Federal resources and Federal support are being allocated.

We must consider the needs of students attempting to pursue their post-secondary education and how we can best assist them in that goal. This goal has to be reviewed in the context of whether it is prudent to continue long-term subsidies for those who have already taken advantage of educational opportunities provides by the Higher Education Act and its many student aid programs that are now in the workforce, reaping the benefits of that education. This is just one of the many questions facing this Committee as we work through the reauthorization process.

This hearing will allow us to learn more about how the Consolidation Loan Program fits into the mission of the Higher Education Act, how it fits into our goals for this reauthorization, that is, increasing access and affordability to students pursuing post-secondary education, and the fairness of the programs being offered.

I am hoping today's discussion provides for a constructive discourse about the program, the different views as to how or if it should be amended, and what is truly best for the students we are trying to help secure a quality education.

I look forward to hearing all of the testimony to be presented here today and to our continued collaboration in addressing the needs of low and moderate income students and in increasing access for these students to an affordable, quality education.

[The statement of Mr. McKeon follows:]

Statement of the Honorable Howard "Buck" McKeon, Chairman, Subcommittee on 21st Century Competitiveness

Good morning. Thank you all for joining us for this important hearing on the Consolidation Loan Program. As we move forward with our efforts to reauthorize the Higher Education Act, we continue to address the many issues within that Act in order to help make postsecondary education a reality for low income students who previously had little chance of pursing such a dream. This hearing is another in our continuing series and is meant to provide information to the members of this Committee about one of the loan programs within the Higher Education Act.

Earlier today Chairman Boehner and I joined together to unveil the principles that will guide the remainder of the reauthorization of the Higher Education Act. When the Higher Education Act was authorized in 1965, its intention was to expand access and provide opportunities to low-income students. Yet today, I believe some higher education programs have lost sight of that original mission—and the crisis of skyrocketing college costs makes it more important than ever to ensure the higher education programs are reaching their full potential to expand access to higher education in America. I believe the principles we have outlined will help us address this crisis, and realign programs under the Higher Education Act to more fully meet the goal of expanding access to a college education. Briefly, these principles are: holding colleges accountable for cost increases; removing barriers, particularly those that disproportionately harm non-traditional students; improving quality and innovation by empowering consumers; and realigning student aid programs to ensure fairness for America's neediest students and families. These principles will guide reforms to all areas in the Higher Education Act, including the Consolidation Loan Program, which is the topic of today's hearing.

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When the program was originally developed, it was done so as a way to address a specific issue - providing for an opportunity to consolidate debt with one holder. While the interest rate structure for this program has changed over time, it has always called for a somewhat higher rate than the underlying loans. It is only because of the recent low variable interest rates that this program has now taken on a mantle of a home mortgage even though it is totally dissimilar.

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We must consider the needs of students attempting to pursue their postsecondary education and how we can best assist them in that goal. This goal has to be reviewed in the context of whether it is prudent to continue long term subsidies for those who have already taken advantage of educational opportunities provided by the Higher Education Act and its many student aid programs and are now in the workforce, reaping the benefits of that education. This is just one of the many questions facing this Committee as we work through the reauthorization process.

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I look forward to hearing all of the testimony to be presented here today and to our continued collaboration in addressing the needs of low and moderate-income students and in increasing access for these students to an affordable, quality education.

I yield now to my friend from Michigan, Mr. Kildee, for his opening statement.

Chairman MCKEON. I now yield to Mr. Kildee for his opening statement.

STATEMENT OF HON. DALE E. KILDEE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Mr. KILDEE. I thank you, Mr. Chairman. I am pleased to join Chairman McKeon at another hearing on reauthorization of the Higher Education Act. Today's hearing is especially important since it deals with the issue of loan consolidation and the ability of students to refinance their consolidate loans.

These are two issues which have garnered the attention of the public and many of our colleagues here in Congress. Our economy, we know now, is struggling. Teachers in many states—California, Washington, Oregon, all those states—are losing their jobs, are going to be pink-slipped. The economic downturn, coupled with the massive levels of crippling debt students incur to attend school, is making it increasingly difficult to pay back student loans.

The question for this Subcommittee should be how do we respond to the needs of these borrowers in a way that is productive for all parties. One of the issues lies in allowing students to refinance their existing consolidation loans and eliminating restrictions on which lenders students can consolidate with.

The existing consolidation programs provide an opportunity for students to combine their existing loans into one loan and therefore 1 monthly payment. Under this structure, students are provided with the ability to reduce the number of payments they make to different lenders and lock in a fixed interest rate for the length of their loans. This fixed interest rate is essential to the financial well-being of the students.

A fixed rate protects students from the volatility of rising and falling interest rates. Unfortunately, current law restricts the choice of students when they seek to consolidate. The so-called single lender rule forces students whose loans are held by one lender to consolidate with that lender. This limits the ability of borrowers to choose the consolidator that would benefit them the most.

Both Chairman Regula and Congressman Wu have been leaders in fighting for the repeal of this provision. Both of these members have introduced legislation to repeal the single lender rule. And Congressman DeLauro has also introduced legislation to allow refinancing of student loans. I hope this Subcommittee can include in the provisions of these bills and report out a bill later this year.

On the issue of refinancing existing student loans, new authority to permit this is important for a number of reasons. Interest rates on student loans are the lowest in 37 years, as low as 3.5 percent or even 2.85 percent if a student is in school or in a 6-month period after graduation.

Allowing refinancing would enable students to access these rates; current law does not. For the average borrower with 17,500 in loans, the difference between a 8 percent and a 3.5 percent rate is $40 per month and over $4,500 in interest savings over the life of the loan. This added debt impacts students in very negative ways as they struggle to buy a home, a car or start a family.

Another answer to rising levels of student debt is to increase the maximum Pell grant. We do not provide enough grant aid to our neediest students. In addition, loans are becoming a greater and greater share of the means students use to finance a college education. And since we began this program, the whole idea was access and while loans are very, very important, the enormity of the debt very often makes that access only theoretical.

We should reverse this trend and dramatically increase the maximum Pell grant over the life of the reauthorization. However, the Committee faces a barrier to enactment of proposals to refinance consolidation loans and increase Pell grants. Instead of focusing on how we can expand student access to post-secondary education through student loans and higher maximum Pell grants, we are focused on tax cuts.

Now the administration has projected that we will have over $455 billion deficit for this current fiscal year, with $475 billion deficit next year. This means that there will be considerably less resources available for expansion of our higher education programs.

This Committee, unfortunately, will have to pick up and choose how we support our higher education programs. These priorities, I really think, are not the proper priorities if we are to remain competitive in the world economy.

In closing, I want to thank Chairman McKeon for assembling this panel of witnesses. I believe the panel is knowledgeable, both the members in the next panel, and I hope that, Mr. Chairman, we can do as well as we did in 1998 in writing a bipartisan bill. That was a great achievement and what we reported out so far, the teacher quality and the loan forgiveness program did go out in a bipartisan way, and I hope we can continue on that path.

Chairman MCKEON. Thank you, Mr. Kildee. We have two panels of witnesses today, and I'll begin by introducing the first panel now.

We're fortunate to have with us two appropriators today. They have been very, very busy, and I think we're farther along on the appropriation process this year than in the 10 years I've been in Congress, probably in the hundred years you've been in Congress—27, excuse me.

[Laughter.]

Chairman MCKEON. But we're happy to have the Hon. Ralph Regula, who is No. 2 on the Appropriations Committee, serves as the Vice Chairman of the Appropriations Committee and Chairman of the Appropriations Subcommittee on Labor, Health and Human Services, and Education. His public service career spans more than four decades, from currently representing Ohio's 16th Congressional district—which I had the good fortune to visit a couple of weeks ago, they're doing some outstanding things there in his district —in the U.S. Congress.

He has previously served as a member of the Ohio House and Senate, also as a teacher and principal—I didn't even know that—in the Ohio public school system, and as a member of the Ohio Board of Education.

And sitting next to him is the Hon. Rosa DeLauro, Democrat from Connecticut, who is serving her seventh term. I've been here

almost as long as you have, but I look like I have been here a lot longer.

Congresswoman DeLauro serves as a member of the Appropriations Committee and its Subcommittees on Labor, Health and Human Services, and Education, as well as the Budget Committee. In 1999, she was elected assistant to the Democratic leader, making her the second-highest-ranking Democratic woman in the House of Representatives.

We are honored to have both of you here today, and you know how these lights work and how the system works, and we'll turn the time over now to Chairman Regula.

STATEMENT OF RALPH REGULA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. REGULA. Well, thank you, Mr. Chairman. And first of all, I want to commend your Committee for the great work you've done. Having been in public education in a number of capacities, I know how vitally important education is to the future of our nation and how important it is to every individual whose, one way or another, life is touched by either his or her opportunities in school as well as parents of children.

And I particularly was interested in your bill on teacher quality. Teachers are the heart and soul of the system and in addressing that problem, you've taken a great stride. I like the No Child Left Behind but I still think the quality of that teacher in the classroom is a key to a good educational experience for every child.

And I think you for holding this hearing today on the issue of student loan consolidation and for allowing me the opportunity to appear before you on this topic. I appreciate the chance to speak with you about this subject and share with you my goal in introducing legislation to eliminate the single lender rule in student loan consolidation. The bill, H.R. 942, is the Consolidation Student Loan Flexibility Act of 2003.

When the House reauthorized the Higher Education Act in 1998, the bill contained no exceptions for loan holders who wished to consolidate their student loans. As I understand it, however, at the insistence of the Senate during the conference, the provision that precluded one specific group of student loan holders from shopping for the best rates on their loan consolidation was retained in the law, those students with multiple loans from only one lender.

This provision has become known as the single lender rule. I believe it is unfair, hence the reason for my legislation, and I ask that in the 2003 reauthorization of the Higher Education Act the exception be removed.

This exception makes no sense and it is unfair to this one group of student loan recipients. It has been argued that unscrupulous lending companies would swoop down and take advantage of these naive students when they are making decisions about managing their student loans, and I find that one very difficult to accept.

Those supporting the exception said that the students need to be sheltered, protected—that's a real vote of confidence in our education system. This implies that there is some magical knowledge that is imparted when you receive loans from more than one lender that isn't received if you get multiple loans from the same lender.

It also implies that the graduates now out in the workforce as teachers, administrators, and professionals are not smart enough to weigh the options before them and make the best decision for their situation. I believe that the graduates of our schools and of higher education are capable of deciding what is best for them, whether they received loans from one lending institution or multiple institutions. With interest rates at historic lows, it is unfair to limit the choices that these recent graduates are given.

More than 22 members of the House agree with me on this position and have cosponsored my bill. Furthermore, this topic has become of interest to other members such as Ms. DeLauro, who have introduced bills that have similar provisions.

Again, I appreciate your interest in this subject and I look forward to an informative hearing this morning. When the Subcommittee drafts its proposal for the reauthorization of the Higher Education Act, I ask your support in eliminating the single lender exception.

And I thank you for the opportunity to be here.

[The statement of Mr. Regula follows:]

Statement of Hon. Ralph Regula, a Representative in Congress from the State of Ohio

Mr. Chairman, thank you for holding this hearing today on the issue of student loan consolidation and for allowing me the opportunity to appear before you on this topic.

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Again, I appreciate your interest in this subject, and I look forward to an informative hearing this morning. When the subcommittee drafts its proposal for the reauthorization of the Higher Education Act, I ask your support in eliminating the single lender exception. Thank you.

Chairman MCKEON. Thank you.

Ms. DeLauro.

STATEMENT OF ROSA L. DELAURO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CONNECTICUT

Ms. DELAURO. Thank you very much, Mr. Chairman, and I, too, am honored to be here with you this morning and ranking member Kildee, and I appreciate the opportunity that you have afforded to my Chairman, Chairman Regula, and I to come and speak with you this morning about this serious issue.

And I want to just say to Chairman Regula that it is an Honor to serve on the Labor, Health, Education, Human Services Subcommittee of the Appropriations Committee. With someone who has had a background in education the way he has, he brings a practical knowledge of these issues and their importance. I think I've told him before that my practical knowledge in the classroom was when I served as a substitute teacher for several years and you know what kind of attention they pay the substitute teachers in school, Mr. Chairman.

But this whole issue of education—and I just will say this as a brief comment and in my own interest. I view education as the great equalizer so that your socioeconomic background, your gender, your religion, your race, your political party, none of that makes any difference. What makes a difference is your God-given talent.

I'm particularly interested because my dad came as an Italian immigrant in 1913. He couldn't speak the language when he came. He paid a price for not being able to speak the language, is that he left school in the seventh grade when both teachers and classmates laughed at him. But he was determined in his lifetime that his only child, his daughter, was going to get the finest and the best of educations no matter what, and struggled hard—both my folks did—to make sure that I had those opportunities.

And I believe that this is the institution that allows us to, quite frankly, make that road a little bit easier for people in order to reach their vision and their goals and realize their dreams.

Finding new ways to expand college access to all Americans I think is the goal that we all share, and particularly this Committee. It starts with making the Higher Education Act more responsive to the needs of families and for all the progress that we've made in increasing the opportunity to receive a college education in America, I hardly need to tell this group that we face serious obstacles. Students face serious obstacles today.

Among the obstacles is the increasing cost of higher education. It's risen nearly 40 percent in the last decade. My state of Connecticut faces a billion dollar budget shortfall, public university tuition is being increased by 14.5 percent at the same time the Connecticut University system is cutting programs and services and reducing the size of faculty.

These trends, as you know, are not unique to Connecticut. I don't know if it was serendipity, Mr. Chairman, Ranking Member, but today's Washington Post front page stories, States Plan Big Tuition Increase, Budget Woes Lift College Costs as Much as 40 Percent. Front page story of the Washington Post, a very, very telling argument and I'd like to put it into the record, if I might.

Chairman MCKEON. No objection, so ordered.

[The provided material follows:]

States Plan Big Tuition Increases

Budget Woes Lift College Costs As Much as 40%

By Dale Russakoff and Amy Argetsinger
Washington Post Staff Writers
Tuesday, July 22, 2003; Page A01

State colleges and universities in every region of the country are preparing to impose this fall their steepest tuition and fee increases in a decade—the latest fallout of state fiscal crises in which most governors and legislatures this year sharply reduced aid to higher education.

Recently announced tuition increases for in-state students of as much as 21 percent in Maryland and almost 30 percent in Virginia over last fall's levels are larger than those in many states, but still well behind increases in states with even larger budget gaps. Tuition and fees at the State University of New York and the University of Oklahoma are rising about as much as those at the University of Virginia, but they are rising 39 percent at the University of Arizona and 40 percent at the University of California.

The pattern marks a reversal from the boom times of the late 1990s, when state tax collections soared and most governors dramatically raised aid to public colleges and universities, which educate two-thirds of the nation's four-year college students. Some states, including Virginia, froze or even rolled back instate tuition; others, including Maryland, kept increases to a minimum.

Like most of their counterparts, Maryland Gov. Robert L. Ehrlich Jr. (R) and Virginia Gov. Mark R. Warner (D) lifted tuition limits in the face of record budget gaps. Tuition and fees at the University of Maryland at College Park will be $6,759 this fall ($1,089 more than last year), and at the University of Virginia, $5,968 ($1,370 more than last fall). In dollar terms, those increases are among the nation's highest.

Governors and lawmakers in several states said they cut state aid to higher education reluctantly, but did so knowing that colleges and universities could raise money from other sources, including tuition.

University officials voiced concern that many lower- and moderate-income students now will be pushed into community colleges or out of higher education because federal financial aid and most state aid programs are not keeping pace with rising tuition. Meanwhile, the job market for young adults is dismal, and more students need to work to afford college.

"It is curious that national and state political leaders are so interested in ensuring access to and quality in K–12 education, yet once you get to higher education, the interest in accessibility seems to fall off," said Charles Hoslet, director of state relations for the University of Wisconsin system, where tuition on flagship campuses is going up 18 percent.

David W. Breneman, dean of the Curry School of Education at the University of Virginia, said the shift represents a largely unacknowledged national policy decision, as states react one by one to the most serious fiscal crises in decades. The effect, he and others said, is to shift the cost of higher education away from states, onto in-state students and their families.

"They're just balancing budgets, and this is the fallout, and nobody is asking, 'What about our future?'" said Joni E. Finney, vice president of the National Center for Public Policy in Higher Education in San Jose.

Some states, including New York, Oklahoma and Washington, are increasing financial aid to cover some or all tuition increases for lower- and moderate-income families, but many, including Maryland and Virginia, made no changes. And several, including Tennessee and Massachusetts, reduced needbased aid, saying the fiscal crisis left them no alternative. The largest federal grant program, the Pell Grant, is not increasing its maximum award.

With the increases, tuition and room and board at many state universities is now more than $10,000 a year. The National Association of State Universities and Land–Grant Colleges found that room and board at major state universities last year averaged a little less than $6,000.

Students interviewed last week in several states had reactions ranging from annoyance to despair, depending on their financial circumstances. Michael Hansen, who faces a $570 tuition increase at Maryland's Salisbury University, where he will be a junior this fall, said he already works two jobs—at the library and delivering Chinese food—to help his parents pay his tuition, and now "will have to work a little harder so that I can remain a member of academia and not a full-time delivery boy at some random Chinese restaurant."

The stakes are higher for University of Iowa senior Mayrose Wegmann, one of eight children of a single mother who earns the minimum wage working at a coffee

shop. Wegmann already has more than $24,000 in debt, works more than 40 hours a week, doubles up with three students in a two-bedroom apartment, does without cable TV and long-distance service and walks rather than driving or riding the bus. She also receives the maximum Pell Grant of $4,000, which isn't going up, although her tuition and fees will increase almost $900 this fall—for a combined increase of 55 percent more than when she was a freshman. She said her options are to work even more hours or go further into debt.

"It's disheartening for anyone from my background to see these increases, because we know how important a higher education is," said Wegmann, a political science major. "We're all working harder and harder to pay our way, but we're not getting a better education. In fact, we're getting a worse education because the time we have to study is so limited."

A survey by the National Association of State Universities and Land–Grant Colleges found tuition rising at public institutions in all 37 states that have responded so far, almost all as a result of state budget cuts. Increases were less than 5 percent in only three states—Montana, New Mexico and Hawaii.

This is the second consecutive year of higher education budget cuts in 24 states, according to the American Association of State Colleges and Universities, and with no sign of an upturn in state revenue, another round is likely next year. Many states have raised tuition two years in a row.

In Minnesota, the state colleges and universities system recently approved 12.5 percent increases for this September and September 2004, which will mean four consecutive years of double-digit tuition increases for in-state students. The legislature increased need-based grants by 17 percent over the past two years, but officials said some financial-aid students still will pay more.

While public colleges are still far more affordable than their private counterparts, unpredictable costs are a growing issue. Karen Kielbasa, who is putting herself through Virginia Tech, where she will be a senior, said she could handle last year's 9 percent increase and this year's 7.6 percent boost—she simply took out larger loans—but was blindsided by the school's decision to raise tuition in the middle of the year by about $400 a semester.

She said she had to double the hours she worked in the campus library and at a horse stable—from 15 to 30 a week—while taking 15 credits.

Elizabeth Hust, who is paying her own way through the University of Wisconsin with financial aid and an almost 40-hour work week, said she cannot afford to finish her five-year program for a bachelor of fine arts degree. With tuition increasing $700 this fall, she said, she will have enough money for only one more year of college and will drop out in the spring, work full-time and finish her degree part-time over the next few years.

Meanwhile, she may profit from her privation. She has reduced her food budget to $40 a month by eating a lot of rice and making her own bread and pasta—a regimen she is detailing in a cookbook for students that she plans to call "How to Survive on Literally Nothing."

Ms. DELAURO. It's unbelievable reading. One of the biggest obstacles to students and families is the high amount of debt they accrue during college and carry with them for decades after they graduate. At a time when young people and families are looking to start out on their own, make a life for themselves, they are finding instead that they are burdened with massive debts that limit their professional opportunities and reduce their quality of life.

Some of you are familiar with the recent article in U.S. Today that chronicled how difficult it has been for Kathy and Jerry Dillon from Georgia to off a $30,000 student loan despite having a good credit rate, no credit card debt and an affordable home loan.

One of the reasons this problem persists for so many families is that the interest rate on these loans can only be consolidated once. As a result, families like the Dillons who consolidated their student loans in 1996 are stuck paying an 8 percent rate. Even though the interest rates are at a historic low today, 3.42 percent, Federal law does not allow borrowers like this family to take advantage of them.

The issue of loan consolidation is an issue that my colleagues, Chairman Regula, Congressman Wu, Congressman Miller and others on this Committee, have worked on for a very long time.

Rising debt, coupled with large debts and little recourse to refinance, are the reasons why I introduced the College Loan Assistance Act. And this came from constituents coming to me at weekly office hours. I stand at a Shop and Shop or a Waldbaum's on a Saturday morning where I do office hours and where young people have come up—this is where I first thought about the issue and, quite frankly, went to my colleagues who sit on this Committee and so forth and said hey, if we can refinance our homes at a lower rate, why can't we refinance student loans at that lower interest rate?

This would allow students that have already locked in at a much higher interest rate to take advantage of these historic lows and consolidate their debt. In addition, the College Loan Assistance Act would eliminate loan and origination fees that are charged to student borrowers. Currently, the government charges student borrowers a fee of up to 4 percent on a loan principal, accruing interest and adding to the burden of a student's debt, in effect a tax on student borrowers.

Along the same lines, I would like to echo the comments of the Chairman of my Committee, and that's regarding the repeal of the Single Lender rule so that students have the opportunity to consolidate their loans with another lender at a lower interest rate. The only thing that I would add to what my distinguished Chairman has said is that I believe we should include increased consumer disclosure to ensure that the borrower is well-informed of all of their financing options.

While we need to find solutions to make student loan debt more manageable, on the other side of that we need to also make sure that college education is more affordable. In the next decade, more than 15.3 million undergraduate students will attend the nation's colleges and universities and they will face an increase of more than 14 percent.

Historically, the Federal Government has played a major role in college tuition assistance with Federal grant, loan, and work-study programs accounting for two-thirds of all available student aid in academic year 2001-2002, 57 billion out of 85 billion. That year, more than 8.3 million students received Federal student aids with an average award of more than $3,500.

One of the most powerful tools we have had to help students has been the Pell grant, which is targeted to the neediest families, providing grants to nearly four million undergraduate students who have an average family income of $17,300. But as the cost burden of higher education has increased dramatically, the strength of the Pell grant has decreased, from covering 84 percent of tuition in 1975-76 to 39 percent today.

The need is particularly pronounced when you consider that, despite gains in overall post-secondary education participation during the past three decades, the rate at which high school graduates from high income families enroll in college is about 27 percentage points greater than for low income families.

The bill that I would introduced would restore the original purchasing power of the program by increasing the authorized level of the maximum Pell grant to $7,000. It increases the maximum grant to make that college dream a reality but it also means that students would not have to borrow as much, in a practical way making reconsolidation and consolidation in general cheaper. Increasing the Pell grant maximum is a common sense idea that is long overdue.

I am hopeful that some of these provisions, which are similar to those in Mr. Miller's recently drafted College Opportunity Act, will be included in the bill reported out by the Full Committee. At a time when we do have serious challenges before us for the coming decades, when the budget cuts in so many areas are imminent, we need to maintain and improve the Federal Government's commitment to higher education. It is that great equalizer. We need to continue to give every motivated student the opportunity to grow and to contribute to our society.

I thank you very much, Mr. Chairman, and our ranking member, for allowing and affording me the opportunity to speak with you today.

[The prepared statement of Ms. DeLauro follows:]

Statement of Hon. Rosa L. DeLauro, a Representative in Congress from the State of Connecticut

Thank you Mr. Chairman and Mr. Ranking Member, and thank you all for this opportunity to testify before you this morning on an issue so critical to the families of this country.

Finding new ways to expand college access to all Americans is a goal I think we all share. I believe that starts with making the Higher Education Act more responsive to the needs of families. But for all the progress we have made in increasing the opportunity to receive a college education in America, I hardly need to tell you that very serious obstacles face students today.

Among these obstacles is the increasing cost of higher education, which has risen by nearly 40 percent in the last decade. In my state, which faces a billion dollar budget shortfall, public university tuition is being increased by 14.5 percent at the same time the Connecticut University system is cutting programs and services and reducing the size of faculty. These trends, as you know, are not unique to Connecticut. These trends, as you know, are not unique to Connecticut, as the front page article in today's Washington Post confirms.

One of the biggest obstacles to students and families is the high amount of debt they accrue during college and carry with them for decades after they graduate. At a time when young people and families are looking to start out on their own, to make a life for themselves, they are finding instead that they are burdened with massive debts that limit their professional opportunities and reduce their quality of life.

Some of you may be familiar with a recent article in USA Today that chronicled how difficult it has been for Kathy and Jerry Dillon from Georgia to pay off a $30,000 student loan, despite having a good credit rating, no credit card debt and an affordable home loan.

One of the reasons this problem persists for so many families is that the interest rate on these loans can only be consolidated once. As a result, families like the Dillons, who consolidated their student loans in 1996, are stuck paying an 8 percent rate. Even though interest rates are at a historic low today 3.42 percent federal law does not allow borrowers like this family to take advantage of them. The issue of loan consolidation is an issue my colleagues Mr. Miller and Mr. Wu have worked on for some time.

Rising debt, coupled with large debts and little recourse to refinance are why I introduced the College Loan Assistance Act, which would allow students that have already locked in at a much higher interest rate to take advantage of these historic lows and consolidate their debt. In addition, the College Loan Assistance Act would eliminate loan and origination fees charged to student borrowers. Currently, the government charges student borrowers a fee of up to 4 percent on the loan principal,

accruing interest and adding to the burden of a student's debt—in effect a tax on student borrowers.

Along those same lines, I would like to echo the comments of my chairman on the Labor HHS subcommittee, Mr. Regula, regarding the need to repeal the Single Lender rule so that students have the opportunity to consolidate their loans with another lender at a lower interest rate. The only thing that I would add to what my distinguished Chairman has said is that I believe we should include increased consumer disclosure to ensure that the borrower is well-informed of all their financing options.

While we need to find solutions to make student loan debt more manageable, we also need to make college education more affordable. In the next decade, more than 15.3 million undergraduate students will attend the nation's colleges and universities an increase of more than 14 percent. Historically, the Federal government has played a major role in college tuition assistance, with federal grant, loan, and work-study programs accounting for two-thirds of all available student aid in academic year 2001–2002—$57 billion out of $85 billion. That year, more than 8.3 million students received federal student aid, with an average award of more than $3,500.

One of the most powerful tools we have had to help students has been the Pell Grant, which is targeted to the neediest families, providing grants to nearly 4 million undergraduate students who have average family incomes of $17,300. But as the cost burden of higher education has increased dramatically, the strength of the Pell Grant has decreased, from covering 84 percent of the tuition in 1975–76 to 39 percent today.

The need is particularly pronounced when you consider that, despite gains in overall postsecondary education participation during the past 3 decades, the rate at which high school graduates from high-income families enroll in college is about 27 percentage points greater than that for low-income families.

The College Loan Assistance Act would restore the original purchasing power of the program by increasing the authorized level of the maximum Pell Grant to $7,000. Not only will increasing the Pell Grant maximum grant make the dream of college a reality for millions of low-income families, it will also mean students would not have to borrow as much—making reconsolidation and consolidation in general cheaper. Increasing the Pell Grant maximum is a common sense idea that is long overdue.

I am hopeful that some of these provisions, which are similar to many of those in Mr. Miller's recently-drafted College Opportunity Act, will be included in the bill reported out by the full committee. At a time when we have serious challenges before us in the coming decades, when budget cuts in so many areas are imminent, we need to maintain and improve the Federal government's commitment to higher education, so that we can continue to give every motivated student the opportunity to grow and contribute to our society.

I would like to thank the Chairman and the distinguished ranking member again for giving me this opportunity today and I look forward to working with the Committee as it moves forward with the reauthorization of the Higher Education Act.

Chairman MCKEON. Thank you very much. I am going to reserve my time and turn the time now to Mr. Kildee.

Mr. KILDEE. Thank you, Mr. Chairman. A question to Mr. Regula. We've worked closely through the years on so many issues where you've been so good. I can recall those lean years where you were able to pull some extra money for Native Americans and I always appreciated that. They didn't always assign me that much money in the budget but you always were very good and you certainly have done much to promote human dignity and I appreciate that.

Criticisms about lifting the single lender rule include that it will destabilize the marketplace. Do you believe those fears are justified?

Mr. REGULA. Well, we haven't said that allowing you to refinance your car or your credit cards or your mortgages could be destabilizing the market and there's a lot more money involved there than in this. And I think it's a fairness issue, just plain and simple. It's fairness.

It's only fair that these students who, in an effort to get their quality of life improved and their opportunities improved, have taken out loans. And it's a great program, but they shouldn't be penalized because the lending agency is able to borrow the money that they use at a much lower rate and all this does is—this high return that they get from students, is enhance their profits. But pure and simple, it is a fairness issue and we're relying on this Committee to correct this injustice.

Mr. KILDEE. Thank you, Mr. Regula. Rosa, you have introduced legislation to allow students to refinance their student loans. You keep the consolidation program at a fixed rate. Why do you think it's important to maintain that at a fixed rate?

Ms. DELAURO. I thank my colleague for the question because I think if you lock in at a lower fixed interest rate and in some cases simplify the repayment of loans by combining multiple loans into one, consolidated loans enables borrowers to lower their monthly payments by extending the repayment period.

This is—I'll go to what the Chairman has talked about. We make this kind of creative financing very—available to families to deal with their homes. What is the reason why that we shouldn't allow for this kind of effort if—you know, owning a home is one of the great American dreams, having an education in which you can contribute to our society in a very productive way has got to be one of the major goals of our society today.

And to allow this in this combination and allow for lower monthly payments, allowing to extending the repayment period, allowing to make it as easy as possible, if you will, with being able to repay, not pay—you know, not not paying but being able to do what you need to do in a way that puts less of a burden and stress on the individual.

If you read the article in today's paper, we've got young people who are going to school with two, three jobs in order to be able to make the increase in tuition costs, leaving little time, as one quote in the article, that—one quote from a young woman, we're all working harder and harder to pay our way but we're not getting a better education. In fact, we're getting a worse education because the time we have to study is so limited.

Let's do something about allowing for people to get a good education.

Mr. KILDEE. You know, my wife and I were in a position financially when my—I had three children in school—in college at the same time.

Ms. DELAURO. Ditto.

Mr. KILDEE. And when my last one graduated, it was like getting a pay raise. But we took a second mortgage out on our home to be able to do that because we didn't want to burden them with debt. And then recently I refinanced my mortgage on my house and that money was used actually for their college education.

So I think both of you make very good sense there, that we do permit this on mortgages on our house and we used that method in order to finance our three children's education at the time, so I think both of you make very good sense on that.

Thank you very much, Mr. Chairman.

Chairman MCKEON. Mr. Carter.

Mr. CARTER. I'm actually going to do double duty here. Mr. Burns wanted me to ask a couple of questions for him because he had to slip out to a markup.

His questions are what exactly is the role of the Federal Government in these loans if we do allow the second reconsolidation and what effect will it have on the taxpayer?

Mr. REGULA. Well, I think the role of the Federal Government is a societal interest in having a well-educated population and giving everybody an opportunity. I'm a product of the GI Bill which enabled me to go to college and probably made a substantial difference in my life and I think that we fund in our Committee, Rosa and myself, the Pell grants because we say we want every young American who wants an opportunity, a chance at the American dream, to get that.

And part of the reason it's a Federal—participation in these programs is that it's to our advantage as a nation to have a well-educated population. And I suspect—somebody did a study on the GI Bill and said it's been paid for many, many times over by the increased productivity of the GIs who took advantage of that legislation and that program, and the same thing is true on the student loans.

Those people that get a loan that has some help on the interest rate are going to repay that loan many times over in increased productivity and increased—maybe better citizenship. And all those things together are good for a nation.

Mr. CARTER. I agree with that absolutely and I happen to be in the situation personally where I have had a kid in college since 1988. I still have two kids in college today. They love it.

[Laughter.]

Ms. DELAURO. They're going to stay as long as they can, Mr. Carter.

Mr. CARTER. I'm going to say to them what my dad said to me when I was in law school—"Am I going to have to burn the University of Texas to the ground to get you out of it?"

[Laughter.]

Mr. CARTER. But seriously, on the question of being able to once again, a second time, refinance. One of the problems that we face in our family as we look at this is that—we deal with a lot of Plus loans—is the situation where they're still not out of school. Although now is the time, if there ever was, to consolidate your loan, is today but I may have a daughter that may still have at least four or more semesters left to graduate. Now she says she's going to med school which means, you know, God knows when—

Mr. REGULA. Another loan.

Mr. CARTER. —and so the point is it would certainly fit my program to be able to reconsolidate twice because as it exists today, I could consolidate existing loans, but then the new loans I wouldn't be able to consolidate? Is that the way the program works today?

Mr. REGULA. They have a one-time—

Mr. CARTER. One-time only?

Ms. DELAURO. One-time only today. What I've proposed is that the college will allow borrowers to refinance more than once.

Mr. CARTER. As many times as they would choose to do to seek the lower rate.

Ms. DELAURO. That's right.

Mr. REGULA. We do it in homes, automobiles—

Mr. CARTER. I think that makes good sense.

Ms. DELAURO. And your point earlier, I think the Federal Government has played a very serious role in education in the United States and I, like you, I believe, believe that that's a—it's a good role to play and we have tried to make that road easier for young people, and it was GIs, et cetera, to be able to get an education which increases a person's earning capacity, all the economic spin-offs of that education, and I think it's high time we take a look at where we are currently and continue to review that and how we do.

Mr. CARTER. And as appropriate, look at this from the practical standpoint of the overall debt that the government is carrying, you feel like this will enhance the ability of the student to actually pay off his debt rather than forfeit—

Mr. REGULA. No question about it, and it's a small part of the national debt but it's probably one of the most productive investments. I like instead of the word debt, investment. We do it with a home. You have a mortgage but it's an investment. And this is what you do. You invest in the young people of this nation and what better place to do it than with these students.

Mr. CARTER. That's our No. 1 asset.

Mr. REGULA. Absolutely.

Mr. CARTER. Thank you, Mr. Chairman.

Chairman MCKEON. Thank you. Mr. Wu.

Mr. WU. Thank you, Mr. Chairman. I just want to agree with our witnesses and make a couple of points, then ask a question or make a request based on our appropriators witness—the status of our witnesses as appropriators.

I think that Chairman Regula is spot-on with his citation of home ownership. I have always thought of home ownership and education as the two appreciating assets that most middle class Americans have access to. That is, most folks can get cars or refrigerators or whatever and they wear out over time. They do not appreciate in value. For most middle class Americans, it is your home, it is your education which have appreciating values over time and these appreciating assets deserve support.

Second, I want to point out that what we're talking about, student loans, is the largest source of assistance in financial aid. It leverages billions of—what Federal subsidy there is leverages billions and billions and billions of dollars in financial aid and I believe that the original intent of a legislation creating these programs was that the interest that one would pay on student financial aid would be among the lowest in one's loan portfolio rather than among the highest. I mean, that's the point of the Federal subsidy.

But with this consolidation process, and perhaps consolidating at an earlier time and now with interest rates diving so low, we have stood the system on its head, in essence, and student loans could be among the higher interest rate loans in one's portfolio.

And I think that the legislation that you all are proposing, that Mr. Davis of Illinois is proposing, Mr. Miller and I and others, along with Mr. Holt on this Committee, we are all moving in the same direction and we look forward to working together to find some appropriate adjustments and incorporate that in the higher education reauthorization so that we can get this done this year.

The request that I have for you all as appropriators is that there is some concern—because of a Federal subsidy involved, whether it's the special allowance payment or otherwise, because of the Federal subsidy involved, that any adjustments for current borrowers, if we assume that there is a fixed amount of total student aid, any adjustment for current borrowers that—making it—giving them additional benefits might come at the price of future borrowers.

That is, students coming through the chain, that benefits for people who are refinancing might come at the expense of people who are in school and borrowing or might come at the expense of people who are applying for Pell grants.

That may be a legitimate concern that can certainly be addressed if we don't look at student financial aid as a fixed pie to be divided among current loan holders, future loan holders or Pell grants, but that we look at the total size of the pie and be willing to adjust that so that we can accommodate this refinancing, which I think is the right thing to do, and also accommodate new borrowers and also people who are applying for grants.

Mr. REGULA. Well, keep in mind that the lenders assemble pools of money which they in turn lend for many different purposes. But their access to money is predicated on the market and therefore the pool that they are using to make the new loans is at a much lower rate and therefore they can give a better rate.

Being fixed in what the existing borrowers pay is a windfall because they're constantly refinancing their pool of available money, whether it's through insurance companies that assemble money or a whole—banks, you name it. And therefore I don't think it would have any impact in a negative way on prospective borrowers but certainly would bring justice or fairness to those that have existing loans.

And I, for the life of me, can't figure out why a student is locked in when we're not locked in on any of the other sources of credit. I'm sure all of you do as I do, you get a letter every day from a credit card company saying come play with us because we're going to give you a better deal and we'll pay off your credit cards and give you a lower rate.

Why shouldn't students, of all people, have this kind of an opportunity?

Ms. DELAURO. I would just echo the Chairman's words and I would also add that, you know, we do put values and priorities on what you spoke about before, Congressman Wu, is what is it that appreciates in value. We have a physical manifestation in a home, we have an intellectual manifestation in a person's ability to succeed through, as I said at the outset, their talent.

We ought to be reassessing that situation all along the continuum as we move forward to find out better ways in which we can allow for that expansion and have our institutions—you know, no one is talking about breaking the—trying to break the bank but

just trying to keep forward and doing what have been standard practices in other ways, which seem to have worked out pretty well.

Mr. WU. Mr. Chairman, if I may have your indulgence just to make a 30-second comment.

Chairman MCKEON. Use it on the panel, if you would, because we're going to have two panels and we're going to have votes between 11 and 12:00, so in the interest of time we're going to have to move on.

Mr. Ehlers.

Mr. EHLERS. Thank you, Mr. Chairman. And before I ask my questions and make my comments, I would like to yield 30 seconds to my colleague from Michigan, Mr. Hoekstra, who has to leave for another meeting.

Mr. HOEKSTRA. I thank my colleague for yielding and I thank the Chair for letting me sit in on at least part of this hearing.

I just want to express my support for eliminating the single holder rule. It's an issue that this Subcommittee in the House sought to repeal in 1998 and I think it's a good idea for us to revisit the issue. I also want to submit for the record, Mr. Chairman, a letter indicating—signed by 73 of our members indicating strong support for strengthening the student loan program and the efforts of this Subcommittee.

With that, I'll yield back to my colleague.

[The information referred to has been retained in the Committee's official files.]

Mr. EHLERS. Reclaiming my time, I am very pleased with the testimony I've heard here and especially Chairman Regula. I wasn't even aware of the problem and it just makes no sense at all and I will certainly do what I can to help incorporate that in any legislation we do.

I also want to comment on the general problem and some issues that were raised. Congresswoman DeLauro, you mentioned placing value in intellectual capital. And it always amazes me that students are so reluctant to take out loans to get an education and my colleagues here have heard me comment that when I was a professor, I always encouraged students to borrow money rather than drop out of school.

They're all worried about, oh, I don't want these debts hanging over my head. My response is simply as soon as you get out of school, you're likely to get married and buy a house and a car and you won't—you'll have a lot more debt hanging over your head for about 40 years. But what's more important, an education or a car?

And furthermore, the education gains in value and helps you figure out your other debts. A car declines in value. So I think we have something to do in order to educate our students as well about how much an education is worth and why it is worth borrowing money to get an education because it's self-financing in the long run.

It's almost an entrepreneurial decision because by getting an education, you are borrowing money to invest in something that will pay back at a rather handsome rate. So I'm very strongly in favor of the student loan program. I would like to increase the maximums.

One other point I'd like to raise, Mr. Chairman, and that is we have to look at some of the regulations dealing with this, too. I'm dealing in an issue with a constituent in my district now, a young girl who shows great promise. She is not a member of our church but we have helped her as members of the church to get an education.

She is very talented in music. She wants to go to college and her mother refuses to sign the financial aid forms and so she cannot borrow money without that. She is now going through the process of emancipation. She has left home and is living with some friends of mine in order to establish her independence so that she can fill out her own financial aid forms.

I don't think the child or a student should have to leave home in order to get a student loan and so we have to look at that aspect, too. Where there is a recalcitrant parent, there has to be some way to waive the requirement.

With that, I believe—

Ms. DELAURO. I would just like to say to my colleague, I thank you for your comment. I think that young people today are being entrepreneurial. As I understand it, with 64 percent of students who have a debt and the average debt is about $17,000 for a 4-year public education, so I think young people are heeding what your advice is.

And the fact of the matter is between 1991-1992 and 2001-2002, average tuition and fees grew by 37 percent in private 4-year institutions, 38 percent in public 4-year institutions. The increase has outstripped 8 percent growth in inflation, median family income over the same period.

I mentioned the average debt is about $17,000 and the National Center for Public Policy and Higher Education reported this past week that students at public 4-year colleges in 16 states were hit with tuition increases of more than 10 percent this academic year.

So I think that tuitions are going up. I think that young people are borrowing and you're absolutely right about investing in an education.

Mr. EHLERS. Well, Chairman McKeon is going to take care of the rising tuition rates.

Chairman MCKEON. Hear, hear.

Mr. EHLERS. But just another aspect of this, students may have $17,000 of student loans. I'm more worried about their $5,000 of credit card debt that they have also acquired at a very exorbitant interest rate and if we need financial education about anything, it's about credit card debt.

I yield back the balance of my time.

Chairman MCKEON. Thank you. Mr. Kind. Mr. Van Hollen.

Mr. VAN HOLLEN. Thank you, Mr. Chairman. I want to commend Mr. Regula and Ms. DeLauro for your initiative here. I think it's an important step toward trying to reduce the costs of education and the burden that many of our students leave college and university with.

This is an issue obviously on the minds of many people. Especially in this last year we've seen dramatic tuition increases across the country. In Maryland, my state, just 2 weeks ago we saw the Board of Regents raise tuitions as much as 21 percent at some of

our public institutions. And as I talk to constituents, this is very much on their minds these days so I appreciate the step you're taking.

Another obviously huge component of this—and it's great to have appropriators before the Committee and have an opportunity to talk to you about this—is the Pell grant. Obviously the loan component is a very important part of the whole picture but the Pell grant, as you've heard from testimony before your community and contact with constituents and others—has obviously diminished significantly in the purchasing power over time from what was, I believe, once around 80 percent to now around 40 percent.

And that's obviously something this Committee is going to be taking a look at in a variety of ways and I'm just interested as to whether or not, as appropriators, given our budget climate but at the same time given the high priority I know that you all attach to this and have spoken eloquently about the fact that investing in our future, making sure that every student who wants to go, who has shown the ability to go to college is not denied that opportunity because of income, that given the fact that that is a priority, what you see the prospects are in the out years for really signif—making a real commitment to significantly increasing the appropriations for Pell grants.

Mr. REGULA. Well, I think that's a real challenge. Since Ms. DeLauro and I have been working together on that Subcommittee, we have increased Pell grants about 15 to 20 percent, recognizing the importance of these to the needs.

I would hope we can continue to do that but it depends a lot on the nation's economy, on the availability of funding. In our Subcommittee, we have such enormous demands in education, in medical research, in labor, that it's tough to sort it out and we've done the best we possibly could with the Pell grants.

Mr. DELAURO. I think as the gentleman knows, a part of the legislation I've introduced would increase the maximum Pell grant award amount to $7,000 thereby trying to do what you've talked about, increasing that purchasing power and allowing further access.

I also happen to believe that then that cuts down on debt and the need for consolidation and the need for reconsolidation. I believe that's the end product of it. And the Chairman has said that, and he has worked in very good faith to try to increase the amount of the Pell grants, I believe we have to take a look at where our priorities lie and where our values lie in this country.

And if we put a high premium on education and understanding that at the Federal level we do about 7 percent of what education is about, so it's not 50, 60 and moving to 70 or 80 percent. We are at a very—you know, it's at a low number, that we need to think about how in fact we do get a handle on our economic growth and what that means in terms of what tax policy is about and how we can in fact utilize our resources and put them in places where we see a tremendous investment and a receipt on that investment dollar.

Chairman MCKEON. Mr. Isakson.

Mr. ISAKSON. Welcome to both of you. Chairman Regula, you know my deep interest in education. I associate myself with your

comparison that the payback is not just in dollars but it's in the productivity and the life of the individual.

However, I want to ask a question because I'm sitting here trying to sort through all of this in my own mind. I spent 33 years of my life selling houses and placed a lot of mortgages, millions and millions of dollars.

Mortgages are quite different from student loans. federally insured mortgages and student loans do have a difference and I want to ask you if there is a—your Committee can get back and maybe quantify something for me.

FHA and VA loans, although guaranteed by the government, are collateralized by a liquidatable asset that more often than not recovers the obligation and that's one difference. Second, they, like student loans, have an income stream. VA loans have funding fees, FHA loans have insurance. So there is a slight difference.

The only subsidy that really takes place is the tax deductibility of the interest on the income taxes by the borrower. In student loans, the guarantee of the collateral is the individual's ability to pay. The inducement to the industry is the government's guarantee, which is significantly most of the loan and its attractiveness also is the subsidy between the lender rate and the loan rate.

So my question is or what I'm wondering about, wanting to accomplish everything the two of you are talking about, have we—and since we have a mandated appropria—this is not an appropriation issue because it's—the money is guaranteed. I mean, we're going to appropriate it out based on whatever the number comes out to be on subsidy.

Have we quantified the amount of money or has the industry quantified the difference that would take place if these consolidations and refinances took place, our subsidy cost went up as far as the government's concern, what impact that would have on appropriations in the years that followed versus if it stayed the same?

Mr. REGULA. Well, I'm not sure that this would have an impact in that the government subsidy is predicated on the numbers that are allocable or allowable under the program. And if the student gets a better rate that reduces their demands on their income and for that particular cost and they can use it for other things which enhances our economy.

And I'm sure that you, as a realtor, always said to the clients you better buy a home because it increases in value. Well, those homes are going to increase in value because we have an educated population that can go out there and earn the money to buy that home and take out the mortgage.

And I'm sure that when you took those people into the bank or the finance company, one of the questions is what's your level of education and they became better risk if they had a higher level of education.

So I think the two go hand in hand. Obviously you don't have a building as a security but more—equally important you have the credibility of the individual and the talent that they've gained through that loan as the bankable asset, if you will, and I'm sure that you had a much easier time with those who are well educated in getting loans for a property they chose to buy.

I don't think this is going to add measurably to the cost to the Federal Government. It simply reduces the amount of spread that the lender gets on this loan which accrues on their profit and bottom line more than it does on any government obligation.

Mr. ISAKSON. Well, I was never at a loss for explaining to somebody why it was a good time to buy a house.

[Laughter.]

Mr. REGULA. I'm sure that's true.

Mr. ISAKSON. Even in 1983 when interest rates were 16 percent. But nonetheless, my concern is like yours. It's also always a good time to get a better education and improve yourself. My only concern would be the financial ramifications or the unanticipated consequences that might impact us, that could later impact what we could increase Pell grants to or what we could do in terms of more affordability for student loans.

Mr. REGULA. I don't think it would be significant.

Mr. ISAKSON. Thank you, Mr. Chairman.

Chairman MCKEON. Mr. Kind.

Mr. KIND. Thank you, Mr. Chairman. I want to thank my colleagues for your presence and your testimony here today. It's such a crucial issue that we're going to be taking up in this session, the reauthorization of the Higher Education Act, the access, the affordability issue. We just need to recognize the importance of making sure that higher ed is an opportunity that all of our students can share in this country.

And it's not just because it makes sense as far as the great equalizer in this country but it makes sense in regards to our geopolitical interests globally and our strategic and security interests globally.

I mean, just last year China graduated four times the number of engineering students than we did in our own country. India is ramping up their higher ed infrastructure and realizing that that is the key to their future. And if we don't recognize this and start leaving students behind, we're going to find ourselves in a less competitive position in regards to technology and biotechnology and everything else that's very important for the future growth and prosperity of our nation.

And, you know, the issues that you're talking about, the consolidation of student loans, I think is something that merits attention. We're going to have to work hard at—we know the state budget crisis from state to state, the tuition increases that are taking place. We have an opportunity in this bill to make some adjustments in order to make up for what is occurring in virtually all 50 states.

In my state, in my Congressional district, the average undergraduate is looking at 16,000 of debt coming out of school. They're looking also at about a $300 per semester increase in tuition fees because of the shortfall in Wisconsin and, you know, 300 bucks here, $300 there, out here it may not sound like a lot but back home, for low income students, that's a huge amount of money and it could make the difference between them going on to school and not.

As far as the loan consolidation proposals that you have, let me just ask you your opinion in regards to where you see the resistance or the concerns or the arguments on the other side of why this

doesn't make sense or why it isn't fair. Why wouldn't there be more support for doing this than what there is right now? Is it different from home mortgages and refinancing and, if it is, in what way?

Mr. REGULA. The resistance is from the lenders, very simply, and it's different because the law says you can only do it once. And all we're saying is let's remove that barrier so that you have the same privilege here you have with your home loan, your credit card, whatever it is.

Mr. KIND. Well, I'm sure in the next panel we're going to have some representatives from the lending institutions and they're not going to claim it's all about money and it's all about the bottom line and the profit. You know. Locking in at 8 or 9 percent today is a great deal but there's got to be something more to it, I mean, from their point of view.

Ms. DELAURO. Well, it will be interesting to find out what it is from their point of view because the Chairman has been eloquent—

Mr. REGULA [continuing]. It's hard to sell.

Ms. DELAURO. And this is helping people to manage debt, helping people not to default on loans, to go back to Mr. Isakson's concern. This is about expanding people's opportunity to be able to have an education. It seems that it has the earmarks of something that we can coalesce around and there are a lot of people on this Committee who have been working on it for a number of years.

There shouldn't be the kind of barriers that may be there now and that's what we'd like to try to work at in order to mirror a program which we believe works very, very well in this country, allowing home buyers to—homeowners to refinance their debt.

Mr. KIND. Ms. DeLauro, I think you articulately stated the trend that has been taking place in this country over a number of years from grant opportunities to a greater reliance on loans and what that is building into the system is a growing mountain of debt for these students just as they're beginning their lives, their careers, their families, that they're going to have to wrestle with for many, many years to come, more so than even many of us who took out loans when we were undergrads or graduates but certainly not to the extent of what we're seeing today.

Has there been any analysis in regards to the cost savings, in regards to the loan consolidation that students may face nationally, how that might reduce their expenses over the long term? Have you seen any studies or any figures along those lines?

Ms. DELAURO. I'm sure there are. I haven't—you know, I don't have them at hand but it would be something we would be happy to take a look at and—

Mr. REGULA. Logic tells you that if you can reduce an eight to a four, there's going to be some savings.

Mr. KIND. Yeah. That's right. Well, thank you very much.

Ms. DELAURO. Thank you very much.

Mr. KIND. Thank you, Mr. Chairman.

Chairman MCKEON. Chairman Boehner.

Mr. BOEHNER. Thank you, Mr. Chairman. Let me thank my dean of my delegation, Mr. Regula, Ms. DeLauro, for coming and offering an opportunity for your proposals to be heard.

There was a discussion of Pell grants and we'd all like to obviously increase the amount of Pell grants considering the ridiculous

increases in tuition. This morning's front page of the Washington Post outlines it pretty clearly and if you understand public institutions and the problems the states are having, you can understand the public institutions' need to raise tuition.

I don't know what that has to do with private institutions who are raising rates are the same level, but they are. And when you consider that one of the real key goals of the Higher Education Act is to expand access for low to moderate income students, it seems like the more we do, the further we get behind.

Now, we've increased the Pell grant 73 percent—the maximum award 73 percent over the last 7 years. Total amount of Pell grant spending, though, has more than doubled because we have more students taking advantage of it and as you begin to look down the road at this wave of students that are coming, even if we don't raise the maximum award, we're going to spend considerably more on the Pell grant.

And let's just say that No Child Left Behind is as successful as we think it's going to be. We're going to have more students, better qualified and able to attend post-secondary institutions.

On the loan side—loan program in 1990 it was a $10 billion a year program. Today it's a $50 billion a year program and by the end of this decade, it will be a $100 billion a year program. But when you step back and look at where the money is going, where the benefits of the program are going, I've begun to ask myself a lot of questions.

And the questions revolve around fairness. Now, fairness is like beauty. It's in the eye of the beholder. But when you think about where the Federal Government is spending its money, where should the benefits go? And I love all this discussion about consolidation and reconsolidation. These people aren't students. They are out of school. They have jobs. They are making money. Some of them are serving here in Congress.

But when you see all the problems we're having granting access to low to moderate income kids, you begin to ask yourself what's fair. Should we in fact shift more of the benefits from the back end of the program toward the front end of the program? Should we be looking at loan limits for freshmen? Should we look at frontloading Pell grants for the neediest of our students?

And as we get through this reauthorization process, I think our goal is to put more light on where the benefits of the program are to be. I love this discussion about debt. We had a young lady here last summer or last fall who was complaining about the $11,000 worth of student loan debt that she had. And I asked her if she had bought a car. She had. How much was the loan? $12,000. And of course I couldn't keep from comparing a $12,000 loan on a depreciating asset as compared with her $11,000 student loan on an appreciating asset.

Now, let's just look at the averages. The average college graduate will make a million dollars more over the course of their lifetime. The average student. The average graduate. The average graduate today also has $17,000 worth of student debt. Now, this is the best deal I have ever seen in my life. I'll take it every day.

You have $17,000 worth of debt that assures you upon average that you're going to get a million dollars over the course of your lifetime in higher earnings.

Now, I don't want to saddle anybody with debt. I don't like debt. I don't have much debt. I don't like living with debt. But what a deal. I think it's the best deal in the world. And so I would—as we spend the rest of this summer and fall getting into this, we ought to talk about what's fair and look at ways to do our job, which I think is to provide more access to highly qualified students.

I do really appreciate both of you being here and putting up with all this.

Mr. REGULA. Mr. Chairman, if I might comment, it would be interesting to calculate the additional income tax that that million dollars is going to generate as compared to the minimal costs of the government's subsidy for the $17,000 loan. Talk about a good deal. That is a superb deal.

Mr. BOEHNER. Good deal for the government, too.

Mr. REGULA. Good deal for everybody because that individual is not only earning more money, he or she is likely to have a greater role in their community and do the things that build quality communities that are vital to the future of our nation.

Chairman MCKEON. Mr. Hinojosa.

Mr. HINOJOSA. Thank you, Mr. Chairman. It's interesting to listen to our great Chairman of the Education Committee and I see things with my glasses slightly different. But thank you, Chairman Regula and Congresswoman DeLauro, for coming to share with us your thoughts on how we could address concerns that students have to be able to access higher education.

Listening to my colleague, Congressman Isakson, talk about his experience with the mortgage industry and selling homes, I wanted him to hear me but unfortunately he left. He talked about the guaranteed loan program for some mortgage holders through FHA and other agencies and it seems to me that what you all are proposing should be guaranteed just like those homes because we are going to be making an investment that is going to make a lot of people enjoy better quality of life and thus reduce the numbers that we are sending to prison.

It will reduce the cost of building those prisons and maintaining those prisoners in prison and just completely reverse it to let them produce hopefully a million dollars and spend it improving our economy and giving us the prosperity that we want.

So as I listened to Congressman Isakson, I was confirming that your ideas of guaranteeing these loans and consolidating them and just allowing that the Pell grant go to 7,000, I heard our Chairman talk about how we have successful increased Pell grants from 1,500 to 3,500 but he didn't say that back when they were 1,500 it covered 80 percent of the cost of going to college, and today the 3,500 only covers 40 percent of what it cost to go to college before the loans that are in the newspaper today, and how the colleges are going to go up from 7 to 25 percent in this year.

All of this to say that what you all are bringing to us here in this Committee has a lot of substance and it doesn't take much to envision how this kind of an investment is going to actually improve the use of our money.

And finally, Mr. Chairman, he said we need to know how we are spending our money, our budget, at two and a quarter trillion dollars. Well, I wanted to tell the Chairman that we just increased the amount that we can owe in the deficit by one trillion, approved that just recently, and we increased the amount that we're going to spend in the military budget from just 2 years ago to 2004 by an additional $100 billion.

So does it make sense that we just continue to be spending the money, the big chunks of money, in the military and in prisons versus in education where you told me that what a wonderful difference it made in your life when GI Bill came into effect?

So I thank both of you for coming and lending some light to what is possible with your legislation and we hope that we can continue this dialog and that we can, in the end, make the right decision instead of the way that we are headed which is a bigger deficit and spending so much money in military and on prisons.

Thank you very much for coming to speak to us.

Chairman MCKEON. Mr. Burns.

Mr. BURNS. Thank you, Mr. Chairman. I appreciate the panel and their input.

Just a couple of very brief questions. First of all, I share with you your concerns for the debt burdens of the students that are out in the academic world and those who are beyond that world. Spending 20 years in that world, I understand the challenges they face.

The cost to the taxpayer in consolidation or reconsolidation, could you address that issue? Do you see a cost to the taxpayer in the proposal that maybe either of you have presented here today? Is there a cost to the taxpayer, additional burden to the taxpayer with allowing students to consolidate or reconsolidate or eliminating the single lender provision? Is there any cost to the taxpayer?

Mr. REGULA. I wouldn't anticipate any great change here. The agreement is between the student and the lending agency.

Mr. BURNS. That needs to be very clear because I think there's a bit of confusion on that issue. If the taxpayer is in any way subsidizing the reconsolidation of a student loan, especially those students who may be beyond the academic environment where we're putting our money now, not into new students getting an education but really into those students who are two, five, 8 years out.

And I agree with you. They should be allowed to take advantage of the marketplace and I want to provide that opportunity. And I was glad to see in the testimony, especially in your proposal, Representative DeLauro, that we had increased consumer disclosure, that they had more information.

But I think the most important thing that we face is if we were to provide this opportunity, which I'm fundamentally in favor of, it must not add a burden to the taxpayer who would reasonably be expected to subsidize or support the new loans, not the existing loans.

So, again, that's my one single question. You do not see any problem with that?

Ms. DELAURO. I don't see a problem with that effort. Obviously it's something that you want to take a look at. My sense of this is just in listening to families and listening when we talk about young people. I think the ability again, as I say, to manage debt, to be

able to lower the cost on default and all of those kinds of efforts, I think add to taking a burden off of taxpayers in this effort.

Do we view that the cost of refinancing your home in the way that we do and we view that now has come to be almost by way of right as what the—

Mr. BURNS. Yeah, but who pays the origination fee and the consolidation fee and those fees associated with renegotiation? Mr. Chairman?

Mr. REGULA. You get deductibility of your interest.

Mr. BURNS. You get deductibility of your interest.

Mr. REGULA. On your home loan.

Ms. DELAURO. On your home loan.

Mr. REGULA. Not even on the student loan.

Ms. DELAURO. You can deduct it. And actually, you're adding—one of the things I had pointed out with the origination fees in some of these other efforts that you really—you know, you add to the—it's almost like a tax to these other folks and with the home mortgage you can deduct those fees.

And we have two separate systems here and what we're trying to do is to see if we can mirror the other. We're obviously willing to take a look at what the issues are but we are clearly open to where there are questions and happy to try to answer them and work them through.

Mr. BURNS. I would support a proposal that would ensure that the taxpayer did not subsidize the refinancing—the reconsolidation and consolidation of student loans and I would also support those measures that would focus these programs on students entering the system so that we frontload it so that more students have opportunities to obtain a college degree and then enjoy the professional benefits of that.

So I thank you for your input and I look forward to working with you on this program.

Chairman MCKEON. Thank you. Mr. Ryan.

Mr. RYAN. Thank you, Mr. Regula and Ms. DeLauro for your leadership, Mr. Regula, also in the State of Ohio, not only for what you do for your district but what you do for all the schools in our state and all the help you've given.

Interesting that the student loan is 3.42 percent and the staff just gave me off the web site for the credit union, annual percentage rate for a new car is 1.2 percent. And it's 3.4 percent for student loans.

I kind of want to bring and make more of a statement. Chairman Boehner stated that $1 million over the course of one's life, should they have a Bachelor's degree as opposed to a high school diploma.

According to most of the tax groups, we say we spend about 40 to 50 percent or our earned income in taxes. So if you would take that number of a million dollars over the course of your lifetime and say you were going to pay 40 percent of that in taxes, that's $400,000 that's going to go back into the government in some fashion on a 17 to $20,000 investment that you're making.

And I agree with the Chairman that that's a great deal and I think that illustrates the point that we have to make these investments and we can't wait any longer. We have to make them now. And I encourage the last group that we had last week when we

were holding the Committee—I know in Ohio, Chairman Regula, that we have a lot of statistics saying that for every dollar that the State of Ohio invests into higher education, they get $1.84 to $2 back in tax money, and that if Ohio would be at the national average for Bachelor's degree, Ohio would have another $2 billion in the state kitty because of the investments that we would have made.

And I made this argument when I was in the State Senate and I want to encourage, whether it's through our Committee or through your Committee, that we fund a study or find someone to do a study to find out what the return on the Federal investment actually is so we can talk in an educated manner about this.

One last point that I want to bring up. I just read an article in the New York Times about IBM moving three million jobs from here, from the United States to India. And these are software design jobs, these are high tech jobs. Oracle is going to increase by 3,000 jobs from here—they're going to increase them in India. Microsoft is going to double their employment in India for high tech jobs.

The only way we can compete—because we can't compete with wages, and I understand this gets into a discussion about trade. And Mr. Tierney made a great point. We made all these deals on trade with the premise that we were going to make investments in education so that our workers would be able to compete.

If we don't do this now, we're not just losing our manufacturing jobs. We're losing our white collar jobs as well, by the millions. And the projection is going to be 3 or $4 million in the next few years.

So my point is the same as I think many people have been making here today. It's not just manufacturing jobs. It's high tech, white collar, computer design, software design jobs. If we don't make the investments that we know we get a great return on now, at what point is it going to be too late? And if we want to compete with these other countries that pay very low rages, we're going to have to compete by having more skills, more talent, more entrepreneurialship than all these other countries.

And it starts, as we've said ad nauseam here today and in this Committee, with funding education. And to me, I can't bring this conversation up without talking about the priorities of the tax cuts that we have in this country compared with the investments that we could make in education.

And I just want to make that point and just encourage you to keep up the good work, especially in the State of Ohio, and ask Ms. DeLauro or Chairman Regula for any comments that you may have on that.

Ms. DELAURO. I want to say thank you to the gentleman for his commentary. I didn't respond to Chairman Boehner and I understand his perspective but there is a whole lot that we could take a look at within the Federal budget that deals with the issue of fairness and you address the issue of tax cuts and I've addressed that in other venues and I'm not going to go into that today—

Chairman MCKEON. Thank you.

Ms. DELAURO. —because I think the heart of what this is about—thank you, Mr. Chairman—I think it's a very, very big issue.

On the other hand, we have—the handwriting, I believe, is on the wall with regard to education and I think if we don't understand this as an institution that has some ability to allow and to assist families in this nation to open up the avenues of education and provide assistance that talks about what Chairman Regula is talking about of not putting restraints or constraints on families and young people to be able to get that education, they want to pay for it, they're not asking for it for free.

And if you read today's Washington Post story and you listen to some of these students, we ought to be trying to say OK, where are we in trying to do something about this. It is a crisis. We have got tuitions rising all over the country. We've got young people—we've got unemployment that's rampant. We don't have the skills that people need in this country to do the jobs and they're going—some of the efforts are going overseas.

Why is it that we focus on how we take the tools at hand and try to say as the Federal Government—and we can't do everything. We don't have the resources to do everything here but we have a role in this effort and what the Chairman is talking about in not repealing that rule, what I am talking about and others on this Committee have talked about is saying let's do what we've done in other arenas. It works.

It has made millions of Americans homeowners and allowed them to do what they need to do in their economic lives. Why do we not want to try to open those avenues in education which I would regard as a higher appreciable asset than home ownership when my intellect and my God-given talent can be promoted to work on behalf of this great nation? That's something that the U.S. Congress ought to be interested in trying to do.

Chairman MCKEON. The gentleman's time has expired. Mr. Tierney.

Mr. TIERNEY. Thank you, Mr. Chairman. I want to thank Mr. Ryan for stealing most of my comments.

That's a point that I often make, as well as Mr. Hinojosa's point about the current value of Pell grants and Mr. Regula, we appreciate the work that you do and the perspective that you bring to education. It's refreshing. And Rosa, you know that we always love the work that you do, too.

I just don't want to add a lot more. I think we've asked this a lot. Let me just say that if we were to eliminate the single lender rule, what could we expect lenders to do in response? Not what they'll threaten to do but—

Mr. REGULA. Well, I think we've seen this. The credit card companies have responded by lowering rates because of competition. Banks have lowered rates. Look at the home mortgage today versus 10 years ago? Automobile rates, just listen to the TV. They practically want to pay you to buy the car anymore.

The marketplace responds, and that's the essence of America that the marketplace makes the decision and I think we're simply saying let's let our students go to the marketplace for the decision and not to some artificial barrier that stands in their way under the present law.

Mr. TIERNEY. I'm dying to hear what our financial institution folks who are always telling me about how great the marketplace

is are going to say to respond to that and that's why I pose that out there.

Can you think of any—because I don't think that you're going to stick around necessarily. Can you think of any fairness argument in respect to their position that we ought to consider?

Mr. REGULA. I'd be interested. I can't conceive of it myself.

Ms. DELAURO. I'll chat with several of you after, because we probably won't be here for that, to find out what's been said.

Mr. TIERNEY. Let me just close by saying I think the important thing here to note is—you know, Mr. Boehner made the comment—and I think it's a good thing that more students are getting out of college. It's a great thing. That's what we've always said, is that we wanted to have more students go further in education and we should expect to make that investment. That's sometimes why the cost goes up and that's not a bad thing.

Look at the money we spent in bailing out the airlines. Look at the money we spent in bailing out savings and loans, in the auto industry. Look at the money that we put into farm subsidies. We should be thinking about that in contrast to the amount that we invest in our future in terms of making sure that our population is better educated, particularly with the comments that I joked with Mr. Ryan about talking about.

We are talking about a global marketplace here where the competition is brutal. The first time that I think we've ever seen where a country like the United States with a fairly well educated populous is competing against countries as large or larger with people as well educated or better educated who are willing to work for so far less.

We had better have some sort of strategy to get our people up to snuff so that they can compete and be as productive.

Mr. REGULA. Well, that's borne out by the fact that many countries in the world make higher education a right, without cost, just as the first 16 years here and I daresay that the vast majority of industrialized countries provide access to higher education at no or relatively small cost. This is because they understand that it's in the interest of society to have a well educated people.

Mr. TIERNEY. Exactly. Rosa, do you want to say anything?

Ms. DELAURO. No, I think he's said it. A society is marked by its educated population, its humanity, its intellect. Those are the things that we ought to be striving for. That's the work of this Committee. That ought to be where our values and our priorities and our goals lie and relieve a lot of—you know, I'm not going to talk about No Child Left Behind but children—but I'm thinking we're leaving a lot of young adults behind today if we don't allow them an opportunity to do it.

They want to do this. They're motivated. They're interested. They don't want to game the system. I believe that it's our opportunity to try to help them to try to reach their—realize their dreams.

Mr. TIERNEY. I'll just close and thank the both of you for the perspective that you bring for the common sense and the approach of trying to get things done as opposed to fight a war every time. Thank you.

Chairman McKEON. Thank you very much. I will not ask any questions in the interest of time. We have a vote call. We will adjourn until 12. Thank you.

[Recess.]

Chairman McKEON. The Committee will come to order. We will now begin with our second panel and our first witness in the second panel will be Ms. Rebecca Wasserman.

Ms. Wasserman is the vice president of the United States Student Association, an organization founded in 1947, which represents students on Capitol Hill with the White House and the Department of Education. She's a recent graduate of the University of Wisconsin - Madison, where she studied political science and social welfare.

Our second witness will be Mr. Dallas Martin. Dr. Martin is president of the National Association of Student Financial Aid Administrators which is made up of 3,100 institutions and 9,300 financial aid professionals. Prior to his current role, Dr. Martin served as director of program planning and administration for the Division of Student Assistance Programs with the American College Testing Program as well as serving a number of years as a college and university administrator and educator.

Next will be Ms. June McCormack. Ms. McCormack is the executive vice president of guarantor services and sales marketing for the Sallie Mae Corporation where she leads the guarantor services business loan and is in charge of their product management for loan consolidation. While working with Sallie Mae, Ms. McCormack has also served as senior vice president for sales management and as vice president of institutional and public finance.

Then we'll have Mr. Barry Morrow. Mr. Morrow is the chief executive officer at Collegiate Funding Services. Previously, Mr. Morrow served with the U.S. Department of Education as the general manager of financial services for the office of student financial assistance and he spent nearly 20 years as the senior operations executive at Sallie Mae.

And finally, we'll have Mr. Paul Wozniak. Mr. Wozniak is the managing director and manager of the Education Loan Group for UBS Financial Services, Inc. He has been involved for over 20 years in financing education loans including all aspects of investment banking for both Federal and private loans. He has served on the Congressionally created alternative index and market mechanism study groups and works with groups such as the Education and Finance Council, Consumer Banking Association and National Council of Higher Education Loan Programs Committees.

Before you begin, I'd like to remind you about the 5-minute rule, that the green light comes on when your time starts, the yellow light when you have a minute left, the red light when your time is up. I'd appreciate if you could adhere to that, and all of the questioners also.

[Laughter.]

Chairman McKEON. Ms. Wasserman.

STATEMENT OF REBECCA J. WASSERMAN, VICE PRESIDENT, UNITED STATES STUDENT ASSOCIATION

Ms. WASSERMAN. Thank you, Chairman McKeon and distinguished Committee members for having me speak on the issue of student borrowing and let's be clear, student debt.

First, let's start with some of the positive aspects of higher education. The Advisory Committee on Student Financial Aid Assistance reports that by 2015, 1.6 million 18 to 24-year-olds will enroll in college and most of them will be low income students.

Of those students, many will be the first to attend college in their families and this will result in college graduates entering our workforce ready to contribute to the economy and this will provide services for our communities. It will also result in college graduates ensuring that their children will have access to college.

However, with increased numbers of students enrolling, particularly low income students, there needs to be an increased commitment to student aid. High student loan debt is sweeping our country and our college graduates are experiencing an average debt of $17,000 in debt. Students are concerned with this growing problem and would like to see this Congress lesson student debt and increase access to higher education.

I am a graduate of the University of Wisconsin-Madison where I, along with many of my classmates, took on student debt. In 2001-2002, there was close to 11,000 borrowers in my college alone. The current borrowing climate is different when both my parents went to UW Madison and they both said that students there used to be able to work during the summer to avoid taking on costly loans. Today, for many if not all students, there aren't enough days in the summer to make that a reality.

USSA supports the programs in place for student borrowers and would like to see them expanded upon. Loan consolidation allows students to lock in a fixed rate on their loans, keep their monthly payments at a manageable level, have one easy monthly bill, and choose between repayment options.

For example, if student borrowers consolidate with the expected new low interest rate, the typical borrower could save approximately $3,200 over a standard 10-year payback period. Consolidation is one tool students can use to lessen the financial burdens that they carry.

Additionally, reconsolidation would allow students to lock in more favorable rates. Ideally students need reconsolidation proposals with a fixed rate that allows them to access the existing historically low interest rates. Members of Congress should advocate for solutions that help student borrowers get out of debt in a manageable way.

However, even with consolidation in place, Congress needs to take steps toward reducing the burden of unmanageable debt for student borrowers. Students are proposing the elimination of origination fees and as well as increasing loan forgiveness programs.

Under current laws, students pay up-front fees with each loan they originate. Origination fees result in less money for student expenses, yet at the same time students are required to pay interest on the full amount of the loan.

Loan forgiveness is also a proactive policy that helps students quickly begin to contribute to the economy instead of being stifled by debt. Additionally, loan forgiveness allows students freedom to choose professions that are critical to our communities.

In a time when we are in great need of those who contribute to our communities by becoming teachers and other civil servants it is important that we are providing important incentives. Loan debt should not decide a student's career path.

I would be remiss, though, if I didn't bring grant aid into this discussion, as the loan debt we have spent the morning discussing is a result of inadequate grant aid. USSA believes that the Pell grant is the best way to increase access to higher education. In the '70's, as we've heard earlier, the Pell grant covered nearly 70 percent of college cost and student loans were merely making up the difference.

Today the situation is very different. Students are forced to take out loans that cover almost 60 percent of college cost while the Pell grant contributes less than 40 percent. It will take leadership from higher education champions to restore the buying power to Pell and students are looking for those leaders.

USSA has worked with students across the country in the past year to develop campaigns for the reauthorization of the Higher Education Act. The main goal of these campaigns has been to strengthen grant programs and to make loan programs less costly. Students hope to be active participants in the reauthorization and we hope to ensure increased access to college.

The time is now for Congress to invest in higher education. States have tight budgets and are making decisions to freeze or reduce higher education spending. This means less money for institutions that receive state funding and less grant aid for need based programs that directly help students. Considering these conditions, Congress must prioritize higher education spending.

These proposals would allow Congress to provide students with a variety of solutions that will lessen student debt. It must remain a priority for this community to help ease the debt burden that students face. We are very eager to see Congress take on this issue.

Thank you for your time and please ask any comments or questions.

[The statement of Ms. Wasserman follows:]

Statement of Rebecca J. Wasserman, Vice President, United States Student Association

Thank you Chairman McKeon and distinguished committee members for having me speak today on the issue of student borrowing, and let's be clear student debt. First let's start with some positive aspects of higher education. The Advisory Committee on Student Financial Assistance reports that by 2015, 1.6 million 18–24 year olds will enroll in college and most of them will be low-income and first generation students. This will result in college graduates entering our work force to contribute to the economy and provide services for our communities. It will also result in college graduates ensuring their children have access to college.

However with increased numbers of students enrolling, particularly low-income students, there needs to be an increased commitment to student aid. High student loan debt is sweeping our country and our college graduates are experiencing an average of $17,000 of debt. Students are very concerned with this growing problem and would like to see this Congress lessen student debt and increase access to higher education.

I am a graduate of the University of Wisconsin Madison where I along with many of my classmates took on student debt. In the 2001–2002 academic year there were close to 11,000 borrowers at my college. This is definitely far more borrowers than when both my parents attended UW Madison from out of state. They have both said that students used to be able to work during the summer to avoid taking out costly loans. Today, for many, if not all students, there are not enough days in the summer to make that a reality.

USSA supports the programs in place for student borrowers and would like to see them expanded upon. Loan consolidation allows students to lock in a fixed rate on their loans, keep their monthly payments at a manageable level, have one easy monthly bill, and choose between repayment options. For example, if student borrowers consolidate with the expected new low interest rate, the typical borrower could save approximately $3,200 over a standard ten-year pay back period. Consolidation is one tool students can use to lessen the financial burden they are forced to carry.

Additionally, re-consolidation, would allow students to lock in more favorable rates. Ideally students need re-consolidation proposals with a fixed rate that allows students to access the existing historically low interest rates. Members of Congress should advocate for solutions that help student borrowers get out of debt in a more manageable way.

However, even with consolidation in place, Congress needs to take more steps towards reducing the burden of unmanageable debt for student borrowers. Students are proposing the elimination of origination fees and more loan forgiveness programs.

Under current law, students pay up-front fees with each loan they originate. Origination fees result in less money for student expenses, yet at the same time students are required to pay interest on the full amount of the loan.

Loan forgiveness is a proactive policy that helps students quickly begin to contribute to the economy instead of being stifled by unmanageable debt. Additionally loan forgiveness allows students freedom to choose professions that are critical to our communities. In a time when we are in great need of those who contribute to our communities by becoming teachers and other civil servants it is important that we are providing important incentives. Loan debt should not decide a student's career path.

I would be remiss if I didn't bring grant aid into this discussion, as the loan debt we have spent the morning discussing is a result inadequate grant aid. USSA believes that the Pell grant is the best way to increase access to higher education. In the 1970's the Pell grant covered nearly 70% of college cost and student loans merely made up the difference. Today the situation is very different. Students are forced to take out loans that cover almost 60% of college cost while the Pell grant contributes less than 40%. It will take leadership from higher education champions to restore the buying power to Pell and students are searching for those leaders.

USSA has worked with students across the country in the past year to develop campaigns for the reauthorization of the Higher Education Act. The main goal of these campaigns has been to strengthen grant programs and to make loan programs less costly to students. Students hope to be an active participant in the reauthorization process to ensure increased access to college.

The time is now for Congress to invest in higher education. Right now, states have tight budgets and are making decisions to freeze or reduce higher education spending. This means less money for institutions that receive state funding and less grant aid for need based programs that directly help students. Considering these conditions, Congress must prioritize higher education spending.

These proposals would allow Congress to provide students with a variety of solutions that will lessen student debt. It must remain a priority for this community to help ease the debt burden that students carry. We are very eager to see Congress take on this issue. Thank you for your time and I look forward to your comments and questions.

Chairman MCKEON. Thank you. Dr. Martin.

STATEMENT OF A. DALLAS MARTIN, JR., PRESIDENT, NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS

Mr. MARTIN. Thank you, Mr. Chairman, Mr. Kildee. I appreciate the opportunity to testify today.

NASFAA welcomes today's hearing on Federal loan consolidation and we support the continued availability of the benefits of loan consolidation for those former students who need it. In supporting loan consolidation, Mr. Chairman, NASFAA should not be seen as supporting all of the developments of the past 2 years associated with this program. In fact, many NASFAA members are very concerned about by the explosive growth in the number and the dollars of loan consolidation.

NASFAA would recommend that the law dealing with loan consolidation revert back to first principles. When loan consolidation was first enacted, its purposes were twofold. First, loan consolidation was intended to help borrowers who had multiple loans from multiple holders getting a single payment to reduce the confusion of writing several checks each month to lenders. Second, and partially an outgrowth of the first reason, was to curtail defaults by reducing monthly debt burden.

It is time to return to those purposes. Nowhere in the Congressional debate of the '80's was it contemplated that loan consolidation would be used as a refinancing mechanism. In fact, the original loan consolidation program carried an interest rate that was 1 percent higher than that imposed on non-consolidated loans.

Our members are also perplexed that some individuals suggest that federally subsidized consolidation loans are just like home mortgages. Obviously, in one case, the person has a tangible, physical asset and in the other, an intangible one. An education cannot be repossessed or resold.

Let us take a closer look at the government subsidies. When one refinances a mortgage to lower the interest rate and monthly payment, the Federal subsidy, that is, the mortgage deduction on your Form 1040, goes down and you pay more in taxes. When one consolidates Federal student loans, one receives a larger interest rate and monthly payment but extends repayment by up to an additional 10 to 20 years over the standard 10-year repayment plan. The interest rate tax deduction goes down, but Federal loan subsidies substantially increase.

While most mortgages are not directly subsidized by the Federal Government, student loans are directly subsidized and that is the critical difference between student loan consolidation and home mortgages. For an example, an undergraduate student who borrowed $17,000 would receive approximately $700 in subsidies over a regular 10-year Stafford repayment term. But if that same person did a consolidated loan for a 15-year period, then roughly $4,200 in additional subsidies would be paid by the Federal Government on that loan.

The average subsidies for a professional school graduate with a $73,500 loan balance would be $3,100 over a 10-year Stafford repayment term as compared to $36,500 for a 30-year consolidation repayment term.

I ask, is it better economic policy to expend scarce tax dollars to help subsidize future needy students or to give even more subsidies to former students? In my mind, this public policy issue is very clear.

Some have also suggested that a market based solution to loan consolidation is appropriate and that we need to repeal the single holder rule. NASFAA opposes repeal of the single holder rule.

First, its repeal will destabilize the student loan system and second it will reduce competition. Repeal of the single holder rule will allow any lending entity to market its loan consolidation product to any borrower. Now, you say what is wrong with that? The answer is that lenders determine their participation in the Federal loan program by anticipating a certain amount of profit depending upon their business plan.

If a borrower can consolidate loans with any entity that successfully markets the former student, then the first holder must relinquish that loan. At that point, the original lender, having lost its loan, will not meet its projected revenue goals, thus eventually such a lender would have no alternative but to stop making student loans altogether.

The second negative effect comes directly from the first. If fewer lenders participate in the student loan market, then naturally the industry will become more concentrated, fewer competitors means students have fewer choices in lenders.

NASFAA also recommends that the student interest rate on all Stafford loans, including consolidated loans, be changed from a fixed to a variable rate. Public Law 107-139 signed by the president last year mandates that student loan interest rates rise to 6.8 percent fixed on July 1, 2006. NASFAA supported that legislation. However, we proposed then that the interest rate cap be lowered to 6.8 percent and that loans continue to have a variable rate instead of retaining a 6.8 percent fixed rate. That continues to be our reauthorization proposal.

We are concerned about the difficulties associated with moving to a higher fixed rate if the current low student loan interest rate environment continues until 2006. Of course, if the July 1, 2006 increase to a 6.8 percent fixed rate is not changed, then eventually even consolidated loans will carry such a rate, making moot today's controversies on loan consolidation.

In conclusion, Mr. Chairman and Mr. Kildee, I would urge you to put the consolidation issue into the context of the purposes of the Higher Education Act and that is to create educational opportunities, because that's what that Act was designed to do.

We would urge you not to spend scarce Federal budget resources on former students who have already been well served and amply taken care of and who are going to have a better prospect at life, particularly in a program that is not need-tested or even targeted upon needy individuals because every dollar spent on loan consolidation is one less dollar that could be spent on needy students in the future.

Thank you for the opportunity to testify here today, Mr. Chairman, and I'll be happy to respond to any questions that you have.

[The prepared statement of Mr. Martin follows:]

Statement of Dr. A. Dallas Martin. Jr., President, National Association of Student Financial Aid Administrators

Introduction

Mr. Chairman and members of the Subcommittee on 21st Century Competitiveness, I thank you for the opportunity to testify today on student loan consolidation.

I am Dallas Martin and I am the President of the National Association of Student Financial Aid Administrators (NASFAA). Formed nearly forty years ago, NASFAA represents student financial aid administrators at nearly 3,100 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 9,300 financial aid professionals whose passion is ensuring that talented Americans have the opportunity to attend a postsecondary institution by providing counseling and financial resources.

NASFAA Reauthorization Recommendations

NASFAA submitted to the Committee its recommendations for reauthorization of the Higher Education Act of 1965, as amended. We believe this comprehensive set of over 100 individual recommendations will go a long way in providing the necessary structure to ensure and extend educational opportunities for our citizens, to target and retarget scarce taxpayer funds in an era of budget deficits, to appropriately deregulate and simplify the financial aid system, to encourage innovation, to reform Title IV programs so that entities do not have unfair competitive advantages, and to assist borrowers by providing both enhanced consumer protections and benefits.

In crafting reauthorization proposals, NASFAA took seriously its obligation to make recommendations that are unambiguously focused on students and educational opportunity. Our recommendations, taken as a whole, set a high standard for you to meet. That high standard, however, will assure a whole range of positive outcomes, especially making certain that no child will be left behind from attaining their dreams for their future and family because of a lack of the financial resources to attend a postsecondary institution appropriate to their talents and drive.

To not meet this high standard will, in our view, put at risk our system of postsecondary education that serves well so many individuals of limited economic means and will put at risk the ability of students to gain the skills necessary to keep American business and industry competitive and at the forefront of innovation in our world economy.

NASFAA Supports a Loan Consolidation Program

NASFAA welcomes today's hearing on federal loan consolidation and we support the continued availability of the benefits of loan consolidation for those former students who need it.

In supporting loan consolidation, Mr. Chairman, NASFAA should not be seen as supporting all of the developments of the past two years associated with this program. In fact, many NASFAA members are very concerned by the explosive growth in the number and dollar volume of consolidation loans. Our members are also concerned that the focus of Congressional discussions of student loan issues appears to be shifting from students to former students.

As you know, a number of bills on loan consolidation have been introduced recently. We also are aware of numerous articles in the media all dealing with loan consolidation. It is truly unfortunate that other urgently needed changes in this reauthorization legislative process are not receiving the same attention. For example, we are not reading about the need to repeal borrower-paid origination fees or to provide other necessary and beneficial changes in the student loan programs; we don't hear much discussion about the grant programs or important other reauthorization issues. What we do hear loudly and clearly are arguments, some of them disingenuous and some of them off the point, about the need for "competition" in the consolidation loan marketplace.

Indeed, our first panel evidences the deep and sincere Congressional interest in extending loan consolidation. Controversy surrounds this matter, as you know. Just last year the White House surfaced a loan consolidation proposal, but withdrew it under intense political pressure. Some possible solutions being considered in this area will certainly help former students who are federal loan borrowers, but NASFAA strongly believes that some of those solutions will consume scarce federal monies that are better expended assisting current and future students. Further, some solutions actually will disadvantage borrowers and have unintended consequences.

We understand that the principal motivation for the interest of many members of this committee in loan consolidation is the increased student debt burden faced by many students and former students. We urge you to look at NASFAA's related recommendations on this subject. We endorse increased grant assistance and increased authorizations for the Title IV campus-based grant and Federal Work–

Study programs; reform of loan repayment options that have not been significantly changed in a long time; an add-on payment for the neediest of Pell-eligible students who have a negative Expected Family Contribution (EFC); changing the student interest deduction to a refundable tax credit to help reduce student debt; and, making the Federal Pell Grant Program a true entitlement. If the goal of this subcommittee is to address student and borrower debt burden, these topics should be on the table and acted upon.

Explosive Growth in Loan Consolidation and Consolidation Loan Marketing

The amount of loan consolidation has risen to unprecedented levels. More than $32 billion consolidation loan volume was realized in 2002, double the amount in the previous year and double the level of the year before, according to The Chronicle of Higher Education. This volume results not only from the opportunities created by the current extraordinarily low interest rates, but also as a result of aggressive and, in our view, sometimes inappropriate marketing efforts.

Financial aid administrators report they have never seen the amount of loan consolidation marketing aimed at borrowers, their families, and, it almost seems, everyone in America. Some of my staff report they have been targeted multiple times with loan consolidation marketing letters and telemarketing phone calls even though they and their children have graduated from college and paid their student loans in full years ago.

Misleading Marketing & Incomplete Consumer Protection Disclosures

Sadly, I must report that a number of these firms eager to sign up loan consolidation borrowers paint the most positive picture, but neglect to tell the whole story. These rosy scenarios tell borrowers that they can lock-in low interest rates and by using other benefits such as making a certain number of on-time payments or using electronic payment methods, borrowers can receive even lower interest rates. While many firms do caution potential loan consolidation candidates on the possible downsides to loan consolidation, others are less than forthcoming with consumer information or do not inform consumers about the "Catch 22s" of their plans.

Some loan consolidation firms give a hard sell to former students telling them that they can reduce their monthly payments by tens or hundreds of dollars and get an unbelievably low interest rate. These firms soft pedal information or, in some cases, do not disclose at all that the borrower's overall debt will climb by hundreds or thousands of dollars, even double or triple what they would have paid compared to maintaining a standard ten-year repayment plan.

Some firms using the current low rate compare the amount saved by loan consolidation to the statutory 8.25 percent interest rate cap thereby inflating such "savings." Some firms, but not all, will suggest that the low interest rate can be reduced even further by offering on-time payment or electronic checkbook deduction benefits, but do not disclose that few borrowers ultimately qualify for such benefits. When one examines the fine print of on-time payments and electronic transfers of loan payment benefits, then all too often the restrictions are so extensive that for most borrowers, such benefits evaporate. For example, some firms tout the fact that former students in their loan consolidation program can prepay their loans, that all prepayments reduce principal, but neglect to say that a prepayment violates their on-time payment standard and, therefore, a prepayment makes one ineligible for their on-time interest rate reduction benefit. One would think the combination of on-time payment and use of electronic payments from a checking account is unbeatable; however for some firms, if a borrower's checking account does not have sufficient funds in a single month to cover the consolidation loan payment, that overdrawn account make the borrower ineligible for both the benefits of on-time payment and electronic debit of a checking account.

Finally, we find poor consumer information regarding some of the other downsides of loan consolidation. Some firms will suggest in their marketing that borrowers retain their federal loan benefits such as deferment, forbearance, and student loan interest tax deduction. They understate or, in some cases, do not disclose at all especially if Perkins Loans are included in consolidation—that certain benefits such as loan cancellation for teachers or nurses or other similar cancellation benefits are lost if one decides to consolidate. Some gloss over the fact that lender-provided benefits are not offered by certain loan consolidation firms. Some soft pedal the idea that interest-free grace periods may be lost. I am not suggesting that the entire loan consolidation industry either uses or condones such practices, but enough do so to be problematic.

A number of you will suggest that we can fix these problems. Perhaps you can, but federal student aid history is replete with examples of solutions that don't work; that are overly burdensome; that are inappropriate; that can be circumvented; or

that are not enforced by federal authorities. What I believe needs to be accomplished in the area of loan consolidation is for the Congress to reassert historical first principles back to when loan consolidation was initially authorized.

First Principles of Loan Consolidation

You all know that in making changes to the Title IV student aid programs, you need to make choices. And, it is true that in making choices, especially in an era of scarce resources, certain decisions will enhance educational opportunities for our citizens and other choices, however well-meaning, will benefit some individuals, but not extend other benefits that are more important to the greater population of students. Your decisions on loan consolidation are choices that underline that distinction.

Our proposal recommends that the law dealing with loan consolidation revert back to first principles. When loan consolidation was first enacted, its purposes were twofold. First, loan consolidation was intended to help borrowers who had multiple loans from multiple holders gain a single payment to reduce the confusion of writing several checks each month to lenders. Second, and partially an outgrowth of the first reason, was to curtail defaults by reducing monthly debt burden. Borrowers who were unable to make monthly payments could avoid default by consolidating their loans to stretch out the repayment time period and receive the benefit of lower monthly payments.

It is time to return to those purposes. Nowhere in the 1980's congressional debate was it contemplated that loan consolidation would be used as a refinancing mechanism. In fact, the original loan consolidation program carried an interest rate that was one percent higher than that imposed on non-consolidated loans. At that time, the interest rate charged on consolidated loans was set by law at the higher of 9 percent or a weighted average of the interest rates on loans being consolidated (rounded to the nearest whole percentage rate). And, I must state that those original purposes successfully assisted in the reduction student loan defaults and the burden on borrowers with impossibly high monthly payments. We should return to those original purposes for several reasons.

In my mind, the most important reason for returning to first principles comes back to my earlier remarks about choices. To retain a consolidation loan program that can be used as a refinancing tool or to expand refinancing options will cost the government large amounts of resources. If we had unlimited money, I might recommend what the witnesses who spoke before me and others suggest in the area of loan consolidation. But we don't have unlimited resources and so you must make choices. And, the choice I urge you to make is to spend those limited resources any new funding or retargeted funding that you might have in this Higher Education Act reauthorization on expanding educational opportunity for current and future students.

NASFAA has made numerous recommendations to help ensure that each American is not denied their dreams through attainment of a postsecondary education due to a lack of funds and we urge your serious consideration of them. Among our recommendations are several that retarget funding or even deny current federal aid to certain individuals. As to loan consolidation, we recommend the committee reform the loan program repayment options. We believe our recommendations will not only make loan repayments easier for those who need relief, but also will eliminate the need for loan consolidation except in very limited circumstances.

The choice I urge you to make is to use those resources for individuals who are seeking or continuing their education. I believe that the wisest use of limited funding is to expend it on better student aid programs and funding at the front end of the educational process for current and future students and not at the back end upon individuals who have already been amply assisted, have successfully completed their schooling, and are gainfully employed and enjoying all of the benefits that accrue to them because thy were provided an educational opportunity.

Consolidation Loans Should Not Be Compared to Home Mortgages

Our members are also perplexed that some individuals suggest that federally-subsidized consolidation loans are "just like home mortgages." Obviously, in one case the person has a tangible, physical asset and in the other an intangible one; an education cannot be repossessed. Let us take a closer look at the government subsidies. When one refinances a mortgage to lower the interest rate and monthly payment, the federal subsidy (the mortgage deduction on your Form 1040) goes down. When one consolidates federal student loans, one receives a lower interest rate and monthly payment, but extends repayment by up to an additional 10 to 20 years over the standard 10-year repayment plan. The interest rate tax deduction goes down, but federal loan subsidies substantially increase. While most mortgages are not directly

subsidized by the federal government, student loans are directly subsidized and that is the critical difference between student loan consolidation and home mortgages. For example, an undergraduate student who borrowed $17,000 receives approximately $700 in subsidies over a 10-year Stafford repayment term and roughly $4,200 in subsidies over a 15-year consolidation repayment term. The average subsidies for a professional school graduate with a $73,500 loan balance would be $3,100 over a 10-year Stafford repayment term, as compared with $36,500 for a 30-year consolidation repayment term.

Again, I come back to my earlier point: "Is it better economic policy to expend scarce tax dollars to help subsidize future needy students or to give even more subsidies to former students?" This public policy issue, in my mind, is very clear. One is a good investment for our future and the other is a needless investment.

Other Negative Policy Outcomes Related to Loan Consolidation

To retain loan consolidation as it currently exists has other ramifications, all of them negative. Borrowers who consolidate loans with repayment periods out to 30 years will repay a total student loan amount of up to double or triple what they would have paid if they had retained the standard 10-year repayment. They are not going to have as much disposable income. They will not have the funds to buy the home of their dreams, automobiles, or other consumer durable goods. Worse than that they are not going to be in a good financial position to save money for their retirement or contribute as much as they might to their children's postsecondary education or be in a position to utilize PLUS loans for their child's education. These are serious considerations for you to ponder; the ramifications of loan consolidation go well beyond the effects on borrowers, lending institutions, and the federal government.

Single Holder Rule

Some have suggested that a market-based solution to loan consolidation is appropriate and that all we need to do is repeal the "single holder rule." Proponents argue that repeal of the single holder rule will open the market up to competition.

NASFAA opposes repeal of the single holder rule for several reasons. First and foremost, we believe that repeal of the rule will destabilize the student loan system and, thereby, reduce competition. Repeal of the single holder rule will allow any lending entity to market its loan consolidation product to any borrower. What is wrong with that you may ask? The answer is that lenders determine their participation in the federal loan program by anticipating a certain amount of profit depending on their business plans. Some merely originate loans and, then, turn around and sell them. Some hold the loans and service them for the entire length of the loan. If a borrower can consolidate loans with any entity that successfully markets the former student, then the first holder must relinquish the loan. At that point, the original lender having lost its loan will not meet its projected revenue goals. So what is that lender to do if it cannot meet such revenue goals? We suggest that no rational business plan can be constructed to meet such an eventuality and, consequently, such a lender would have no alternative but to stop making student loans altogether. We believe this is not only a real possibility, but one that will quickly become a reality leading to massive disruption and instability in the student loan marketplace.

And, stemming from this fact, let me state my serious doubts that any lending entity involved in loan consolidation from the most reputable to the least caring about borrowers would support a change in the law that would allow any borrower to refinance their consolidation loan once or again and again (reconsolidation). My educated guess is that they would support continuation of current law providing that loan consolidation can only occur once. To allow multiple refinancing, as is true in the case of home mortgages, would financially devastate such loan consolidation lenders. Certainly, the generous add-on benefits would be eliminated.

The second effect comes directly from the first one. If fewer lenders participate in the student loan market, then, naturally, the industry will become more concentrated. The student loan industry is already highly concentrated with a few giant lenders dominating the field. NASFAA has no doubt that a concentrated industry obviously leads to less, not more competition. Fewer competitors mean students have fewer choices in lenders.

In sum, we believe that repeal of the single holder rule will lead to an undesirable destabilization of the loan industry, to less competition and greater concentration in the industry, and, eventually, to greater disparities in borrower benefits and the services offered by the industry. We strongly urge no change in this matter.

Perkins Loan Clarification

Another issue associated with loan consolidation relates to the application of the "single holder rule" with regard to Federal Perkins Loans. NASFAA recommends a clarification so that it is clear that Perkins Loans may continue to be eligible for inclusion in a consolidation loan, but are not treated as a separate "loan holder" to get around the single holder rule. Some loan consolidation firms, in our view, have been violating the law and circumventing the single holder rule by claiming a Perkins Loan held by a school is therefore a separate holder. Consequently, such firms have been consolidating loans in violation of the single holder rule. We believe a clarification is necessary.

A Variable Interest Rate on Consolidation Loans

NASFAA recommends that the student interest rate on all Stafford Loans, including consolidation loans, be changed from a fixed to a variable rate. We understand this position is an evolution in our thinking since we joined with our sister associations in opposing the Administration's proposal to implement a variable rate loan last year. But, in rethinking the whole issue of loan consolidation and student loan interest rates we have come to the conclusion that consolidation loan interest rates should parallel regular Stafford Loans.

We note that P.L. 107–139 signed by the president last year mandates that student loan interest rates rise to a 6.8 percent fixed rate on July 1, 2006. NASFAA supported this legislation; however, we proposed then that the interest rate cap be lowered to 6.8 percent and that loans continue to have a variable rate instead of retaining a 6.8 percent fixed rate. That continues to be our reauthorization proposal. We suggest to the subcommittee that the subject of interest rates is an important one. We are concerned about the difficulties associated with moving to a higher fixed rate if the current low student loan interest rate environment (now at 3.42 percent) continues until 2006. Of course, if the July 1, 2006 increase to a 6.8 percent fixed rate is not changed, then eventually even consolidation loans will carry such a rate making moot today's controversies on loan consolidation. Finally, if consolidation loan interest rates are changed to variable ones and Stafford Loan interest rates are maintained as variable, then the only reason for consolidating a loan is to get a single payment in the event of multiple loans from multiple holders or to extend the repayment time period to receive a lower monthly payment to avoid a default.

Other Consolidation Issues and Recommendations

Mr. Chairman and members of the subcommittee, NASFAA has recommended two other loan consolidation related changes in the Higher Education Act. To reduce loan consolidation costs to the government, we recommend consideration of a "loan consolidation fee." We have not recommended the amount of the fee or the nature of such a fee, i.e. a percentage or flat figure. Second, as part of a comprehensive set of recommendations to level the playing field between the loan programs, NASFAA suggests there is not a need in either FFELP or Direct Loans (DL) for an in-school consolidation benefit and so would eliminate it from the DL program.

Consumer Information

As I referenced earlier, some would suggest that increased student consumer information requirements be mandated for consolidation loans. NASFAA does not believe this is a wise decision. Consumer information disclosures on loan consolidation are included in the counseling requirements that schools and others are required to perform. Financial aid administrators are already diligently helping former students who seek information on loan consolidation and they assist thousands in making informed decisions on whether to consolidate or not consolidate their loans. I must frankly state we are doing as much as we can to inform and provide educational materials to our students and former students. Financial aid administrators know that providing excellent counseling is one of their primary jobs. We oppose any further extension of loan counseling activities or mandates since they would be duplicative of current legal requirements.

In conclusion, Mr. Chairman and members of the subcommittee, NASFAA urges you to put the consolidation issue into the context of the purpose of the Higher Education Act: to create educational opportunity. We urge you not to spend scarce federal budget resources on former students, especially in a program that is not need-tested or even targeted to needy individuals. Every dollar spent on loan consolidation is one less dollar that can be spent on needy students.

Thank you for the opportunity to testify here today. I look forward to working with you, Mr. Chairman, and all members of the subcommittee to reauthorize a Higher Education Act that meets the needs of students, their families, and all of

the parties involved in the delivery of student aid dollars in this nation. I hope that those of you who have not yet reviewed NASFAA's Higher Education Act reauthorization proposals will do so by visiting http://www.nasfaa.org/publications/2003/gnasfaadetailedreauthrecs070903.html

I would be pleased to respond to any questions you may have.

Chairman MCKEON. Thank you.

Ms. McCormack.

STATEMENT OF JUNE M. McCORMACK, EXECUTIVE VICE PRESIDENT, SALLIE MAE

Ms. MCCORMACK. Good afternoon, Chairman McKeon, Ranking Member Kildee and members of the Subcommittee. I am June McCormack, executive vice president at Sallie Mae. On behalf of our 7,000 employees, thank you for the opportunity to speak with you today about loan consolidation.

Sallie Mae is proud to be part of a unique public/private partnership, the Federal Family Education Loan Program. Through this program, $50 million of private capital is leveraged each year by a government guarantee that costs taxpayers very little, a small fraction of that, and as a result, ensures access to millions of students to college.

While we support reform of the loan consolidation program, we oppose reconsolidation and repeal of the single holder rule. These proposals may sound pro-consumer on the surface, but they threaten the student loan program that Congress has successfully stewarded. Our position is shared by most lender and school groups who agree that these proposals will introduce massive new long-term costs and do nothing to improve college access.

As you indicated, Mr. Chairman, the seeds of today's challenges in the loan consolidation program were sown when Congress changed student loans from fixed to variable rates in 1992 and did not make a corresponding change to consolidation loans. Understandably, no one foresaw the rate mismatch that unintentionally makes consolidation loans far more attractive than the original underlying loans.

Student loans are made at variable rates and reset annually based on the 3-month Treasury bill rates. Meanwhile, consolidation loans are made at fixed rates which lock in the same 3-month Treasury rate for up to 30 years. That means consolidation borrowers are locking in long-term loans at even better rates than the U.S. Treasury pays.

Sallie Mae has a strong record of counseling our borrowers. When interest rates were higher, we discouraged borrowers from locking in unless they needed to stretch out their payments. That was Congress's original intent for consolidation. It was never intended to be a refinancing program.

While we now run national education campaigns to educate our consumers about the record low rates, we believe Congress should consider the long-term price tag of extending this benefit to all borrowers all the time. There are two major policy questions that Congress should address as part of consolidation reform in the higher education reauthorization.

First, how does today's loan consolidation program increase access? In today's student loan program, the government subsidized

the cost between the borrower-paid rates and market rates. We estimate that 40 billion in student loans consolidated last year will add over 5 billion in taxpayer costs. If the same volume consolidates this year at today's lower rates, it will cost taxpayers an additional $9 billion. This is not a lender cost. And think of how many Pell grants this could fund.

This new subsidy is not based on need. Does it make sense to need-test the program when students apply for financial aid and then confer deep subsidies after graduation regardless of need? Would reconsolidation strengthen the student loan program? No. It would have the opposite effect.

Now, some people may try to tell you that reconsolidation will save the government money. That's wrong. Just letting everyone who previously consolidated have one more chance to consolidate, just one more chance, would cost the government well in excess of $15 billion, even net of any additional fees that may be generated.

That doesn't begin to contemplate the price of inviting all borrowers to reconsolidate all the time. Reconsolidation will become the giant that swallowed the student loan program.

Furthermore, it will create market instability. Most lenders enter into hedging and securitization contracts to fund future loans. Because of these contracts, Congress has never significantly changed the terms retroactively. If Congress breaks the terms of legally binding contracts, it will send a clear message that loan terms can be changed at any future point thereby increasing the cost of financing every student loan.

We know that some of your constituents are asking if I can refinance my home, why can't I refinance my student loan? And as Congresswoman DeLauro and Congressman Kildee indicated, on the face, this argument makes sense and we're all sympathetic to those who locked in at higher rates.

The reality is, though, that there are enormous differences between student loans and home mortgages. Mortgage lenders set their own rates and build in the risk of repayment. They charge borrowers points and fees. They do credit checks and require collateral and they adjust rates based on credit. Student loan providers can't do any of those things.

If Congress wants to send the student loan program down the road to commercialism, it has to go all the way down that road but its imprudent to offer the benefits of a free market system unless you create a free market system.

Finally, I also want to say a word about proposals to repeal the single holder rule. Repeal of the single holder rule is a solution in looking—in search of a problem. The financial aid community and Congress depend on us to provide capital, pay up-front fees and invest in technology that processes loans and data in seconds.

Without the assurance provided by the single holder rule, lenders would be incented only to be in the consolidation business, not the student loan business. Like reconsolidation, repeal of the single holder rule will do nothing for the student loan program or existing students other than unleash an avalanche of spam, junk mail and telemarketers, some pushing misleading information.

So what should Congress do about loan consolidation? First, provide better and more flexible options to borrowers who are paying their loans.

Second, ensure that borrowers retain their original interest rate structure when they reconsolidate so that those who want or need consolidation do not have to become arbitrage experts and won't risk locking in consolidation rates that may not look attractive in hindsight.

Third, create consistency for direct and FFELP consolidation loans.

Fourth, require borrower counseling to ensure that borrowers fully understand the pros and cons of loan consolidation. And fifth, retain the single holder rule.

Finally, as I mentioned at the outset, we all have to remember what this program is here for and what Sallie Mae was created for, and the answer is access.

Thank you for the opportunity to talk to you today. I would be pleased to answer any questions.

[The prepared statement of Ms. McCormack follows:]

Statement of June M. McCormack, Executive Vice President, Sallie Mae

Good morning Chairman McKeon, Ranking Member Kildee and Members of the Subcommittee, I am June McCormack, Executive Vice President at Sallie Mae. On behalf of more than 7,000 employees of Sallie Mae, thank you for the opportunity to talk with you about the federal student loan program, and, in particular, the loan consolidation program.

On a personal note, it is an honor for me to be here because nearly 20 years ago, one of my first jobs at Sallie Mae was building one of our earliest loan consolidation programs. Today, I manage a very different loan consolidation program for Sallie Mae. I would like to describe recent trends in loan consolidation and recommend some positive steps that Congress can take as part of reauthorization of the Higher Education Act (HEA). I know we share the same goal: To preserve a remarkably successful, stable and cost-effective student loan program that provides $50 billion each year to finance postsecondary education for students.

As described below, we support reform of the loan consolidation program in the upcoming HEA reauthorization. We are, however, particularly concerned about recent proposals that would permit reconsolidation of loans made to borrowers who have graduated, and who already received the benefit of taxpayer-subsidized below-market interest rates.[1] The capacity of our nation's financial aid system to ensure postsecondary access to all of the projected incoming low-income and minority students in coming years is jeopardized by such proposals which would shift taxpayer subsidies from students in school to borrowers in repayment. Moving in this direction also undermines the public/private partnership through which lenders invest private sector capital in support of one of the most successful government programs in history. Never before has the federal government retroactively changed the contract terms of student loans in a significant way after they have been made. This type of retroactive change creates new and real risk that increases the cost of financing and makes the prospect of investor-driven litigation likely.

The policy questions raised by this discussion are difficult and we appreciate the concerns raised by borrowers who consolidated at rates higher than the current market's historically low rates. While we sympathize with their concerns, given today's tight fiscal environment, policymakers will be asked to determine when should borrowers receive the benefits of taxpayer-subsidized below-market interest rates? When they are in school or after they have completed school and are better economically situated to repay their student loans? For example, if all current consolidation borrowers refinanced at today's record low rates - and why wouldn't they - the esti-

[1] The federal guarantee backstopping every student loan ensures that every borrower, irrespective of credit history or when they borrow, pays interest rates that are well below private market rates for unsecured credit. Even in today's record low interest rate environment, the average interest rate on unsecured personal credit is 13%. By contrast, many borrowers who are in repayment currently pay 3.42%. Borrowers who are in school, in grace or in deferment pay only 2.82%.

mated cost to the government, and ultimately taxpayers, would be more than $15 billion.

Late last year, Sallie Mae joined the Consumer Bankers" Association, the Education Finance Council, the Student Loan Servicing Alliance and the National Council of Higher Education Loan Programs in recommending to this Committee how the reauthorization of the HEA can strengthen the student loan program. A copy of these proposals is attached to my testimony. While there is not always unanimity among loan providers and schools, there is nearly total agreement among loan providers and schools that permitting reconsolidation or repealing the "single holder rule" would adversely impact the student loan program. Enacting such proposals would not provide access to a single new student. These proposals also threaten the ability of loan providers to continue to partner with the federal government in making billions of dollars in low-cost capital available each year to students and families to help pay for college. Repeal of the "single holder rule" will do nothing for the student loan program, or existing students, other than unleash an avalanche of spam, junk mail and telemarketers on unsuspecting borrowers.

Background

Nearly 40 years ago, Congress created one of the most successful federal programs in our nation's history—the federal student loan program. Thirty years ago, Congress created Sallie Mae to help make equal access to higher education opportunity a reality. Sallie Mae's mission was to build a stable market where none existed by encouraging private sector loan providers to offer student loans and thereby open the doors of college to millions of students. Thanks to the leadership and vision of a succession of Congresses and Administrations, student loans are available today to any student or family, without a credit check or collateral, so that no child is turned away from higher education based solely on the financial status of his or her family. That entitlement is central to the American Dream. It is the envy of other nations.

We are part of a unique public-private partnership—the Federal Family Education Loan Program, commonly known as FFELP. Last year, loan providers made $50 billion in private capital available in the form of student loans to over five million students and their families at more than 6,000 postsecondary institutions across the nation. The federal government also makes student loans through the Federal Direct Loan Program (FDLP).

The federal student loan program is an unparalleled success story of which Congress should be proud. Since 1965, more than 50 million students have gone to college, in part, thanks to federal student loans. Each year, lenders provide more capital to students, yet the total cost of the FFEL program has declined. Last year, FFELP spending accounted for less than 1/10th of 1 percent of the government's annual $2 trillion in spending. In fact, last year, the federal government spent less than one penny for every outstanding student loan dollar. Equally impressive is the fact that over the past 10 years, entitlement spending increased by 33% while spending on FFELP decreased by 83%. These cost savings are due to the efforts of loan providers, in partnership with Congress and schools, to reduce defaults, increase collections of defaulted loans and reduce costs for interest and other expenses.

Sallie Mae is the nation's leading private sector provider of higher education financing with over $83 billion in student loans and more than seven million customers. We take our responsibilities to students, families, schools and taxpayers under the Higher Education Act very seriously. As the original—and, at the beginning—the only provider of consolidation loans, we are proud to be the number one provider of consolidation loans to borrowers today. Last year, we helped more than 312,000 borrowers consolidate nearly $10 billion in federally guaranteed student loans.

The student loan program is successful because, in an era of limited government resources and rising college costs, America's student loan providers use private capital to invest millions of dollars in services and systems that directly benefit students, their families and schools. This year, Sallie Mae alone will invest more than $150 million in technology support for the student loan program. In recent years, loan providers have developed Internet-based services that provide fast, reliable services for borrowers. Thanks to these investments, students can now receive their loans on the same day they apply—all at the click of a mouse. Only a few years ago, this same process took weeks. Loan providers are also adding web-based tools and services every year that allow students to quickly and easily estimate their college costs, compare repayment options, check their loan status, learn about managing debt and obtain information on debt counseling.

Schools also benefit from investments made by loan providers. For example, we offer financial aid delivery tools to schools that allow them to originate loans quickly and with less paper, answer questions from parents and students, provide one-stop service for students, and give schools greater access to, and control of, loan information. We also complement the efforts of financial aid officers and high school guidance counselors to promote the availability of financial aid by answering millions of calls from parents and students about the financial aid process. We help reduce the cost of college by offering borrower benefits and interest reductions for on-time payment. Finally, we are answering the growing demand for private credit that helps bridge the gap between financial aid sources (including federal loan programs) and available family resources.

So how does this type of private sector investment help real people? It means that if a parent is filling out their financial aid forms and gets stumped on how to answer a question, they can call Sallie Mae's "Parent Answer" line and we will help them. Or if a student decides to enroll at the last minute, thanks to our investment in technology, he or she can have a student loan processed in minutes. It also means that we work with borrowers to help keep them on-time and in repayment, thereby avoiding the consequences and costs of default.

Our ability to invest in our nation's financial aid system is made possible by the historic stability in the federal student loan program that Congress has carefully managed. Proposals to fundamentally alter the student loan program—some even retroactively—not only threaten our ability to make future investments, but will depress the innovation that has made the student loan program the success that it is today.

The Origin of the Loan Consolidation Program

In 1981, Sallie Mae proposed, and Congress enacted, an amendment to the Sallie Mae charter to permit development of a loan consolidation program. The original purpose of the program was to help solve problems faced by an increasing number of borrowers whose loans were "split" between different loan providers. At that time, students who did not accurately navigate changes in their borrower status faced administrative confusion and red tape (requesting deferments from 3 or 4 different lenders and writing 3 or 4 checks a month), and in some cases, even ended up in technical default.

From the beginning, loan consolidation was designed to prevent defaults and simplify repayments. It was never intended to be a refinancing vehicle. In fact, consolidation loans for the earliest borrowers carried an interest rate that was the weighted average of their original loans, rounded up to the nearest whole percent. By offering borrowers the administrative convenience of making a single monthly payment to a single loan provider, policymakers believed that they could reduce the incidence of borrowers defaulting simply because they were unable to keep track of their original loans. Consolidation also provided borrowers with the opportunity to reduce monthly payments by extending their repayment period over a longer period of time.[2] In 1986, responding to requests of other loan providers, Congress authorized all other loan providers to make consolidation loans.

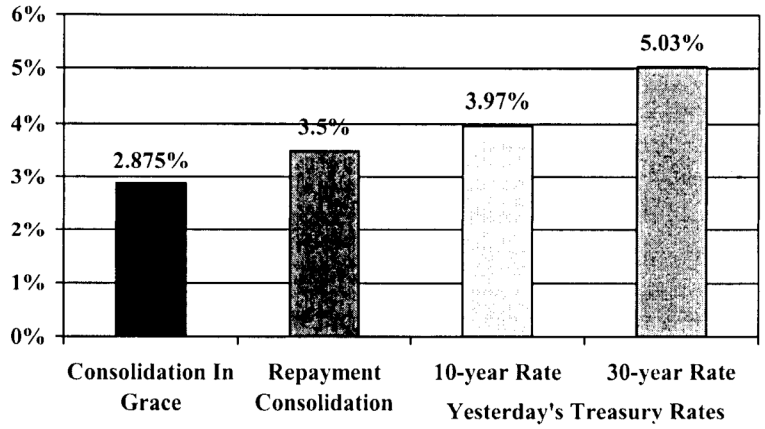
Loan Consolidation Today

Sallie Mae has an excellent record of advising our customers about consolidation. When interest rates were higher, we discouraged consolidation unless a borrower needed to stretch out his or her payments. As interest rates plummeted and consumers started using consolidation as a refinancing vehicle, Sallie Mae made all of its customers aware of historically low interest rates, running national education campaigns.

So, how did consolidation become a refinancing program? The seeds were sewn when Congress shifted student loans from fixed to variable rates in 1992 and neglected to make a parallel change in consolidation loans. As a result, while all student loans made after 1992 have variable rates that reset annually based upon 3-month Treasury bill rates, consolidation loans have fixed rates, which lock-in the very same 3-month Treasury bill rate for up to 30 years. Simply put, today's consolidation borrower is taking out a long-term loan based on short-term rates—an enormous interest rate risk that is borne by taxpayers. In fact, this formula allows a borrower today to pay a rate of interest that is below the United States Treasury's long-term cost of funds.

[2] It is important to note, however, that by extending payments up to 30 years, in normal interest rate environments, many borrowers end up paying more in total interest than they would have had they repaid their loans within the standard ten-year repayment period.

Consolidation Rates Are Below Federal Borrowing Costs



Source: July 16, 2003, Treasury rates from Federal Reserve and from Department of Treasury.

Granting every borrower the opportunity to borrow at rates well below where even the Federal Treasury borrows will drive up the cost of the student loan program. Most of the additional federal cost will go to benefit borrowers who have received post-graduate training.

While many of our consolidation borrowers have smaller balances (Sallie Mae's minimum balance for consolidation is below that of most major consolidation marketers), the majority of our consolidation volume is in higher balance, longer-term loans. Fifty percent of our consolidation loan volume is made up of loans with balances in excess of $40,000 that will be paid back over 25 years or more. Eighty percent of our consolidation loan volume is made up of loans with balances in excess of $20,000.

This distribution has significant implications for cost, because taxpayers will continue to pay the difference between the below-market, subsidized borrower rate and current market interest rates for the entire life of these loans[3]. Comparing who benefits from the additional taxpayer cost, we see that over 60 percent of federal subsidies will go to borrowers with balances greater than $40,000—there are very few undergraduates at this level. Less than 13 percent of the additional consolidation subsidies will go to the typical college graduate, who can only exceed $20,000 if they are independent (generally, over 24 years old) or borrowed at the maximum for five years or more.

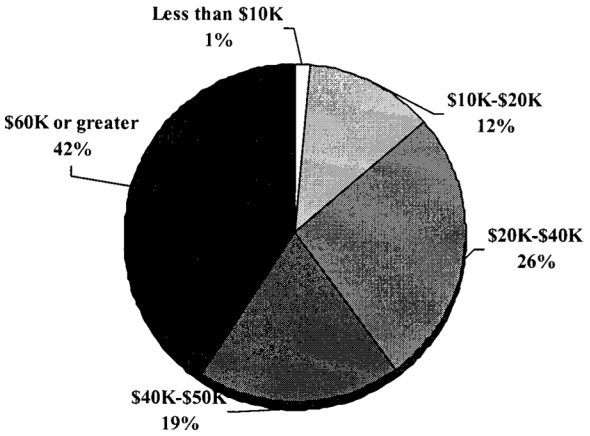
How Much Can Students Borrow?

Total Borrowing Limit	Dependent student	Independent student
Undergraduate	$23,000	$46,000
Graduate	$65,500	$138,500

Source of chart: Expected government subsidy, offset by 1.05% annual fee, by amount consolidated over life of loan; distribution of subsidies based on distribution of Sallie Mae consolidations (1/03 to 6/03); subsidies estimated on net present value basis, using June 2003 Blue Chip Consensus interest rate forecast.

[3]The Congressional Budget Office forecasts that within several years, the net rate to lenders will be 7%. This reflects the offset fee paid annually by lenders of 1.05%.

Where Do the Consolidation Subsidies Go?
Federal Subsidies by Consolidation Balance



61% of taxpayer subsidies will go to borrowers with balances over $40,000; only 13% of the subsidies will go to typical college graduates, who have balances of less than $20,000.

Reconsolidation

As interest rates have declined, borrowers who already exercised their consolidation benefit have understandably raised their hand to complain that they are not eligible to consolidate now to take advantage of the much lower current rates. Quite reasonably, they are asking, if I can refinance my home, why can't I refinance my student loan, too?

On its face, this argument makes perfect sense. And we are sympathetic to those who have locked in at higher rates. The reality is that this argument ignores the enormous differences between student loans and home mortgages.

First, a home mortgage can be refinanced at the will of the homeowner, and therefore there is a high probability that the borrower will pay off the loan early. This prepayment risk is built into the cost of that mortgage. The pricing on a student loan asset, on the other hand, is set by federal law, and makes no provision for multiple refinancings. Under the terms of today's program, a borrower is permitted to consolidate his or her loan only once.

There are other fundamental differences between consolidation loans and home mortgages. For example:

- Homeowners put their homes up as collateral for their mortgages.
  - Consolidation borrowers put no collateral at risk.
- Homeowners pay points and fees to mortgage lenders to refinance their mortgages.
  - Consolidation borrowers pay nothing—the federal government and lenders absorb all costs.
- The rate of interest on a mortgage varies daily, is set by the market, and varies widely depending upon an individual's credit history and the term of the loan.
  - The interest rate on a consolidation loan is set by Congress using short-term rates and is determined in exactly the same manner for every borrower, irrespective of credit history.

Key differences are highlighted in the table attached to my prepared testimony.

We oppose reconsolidation for three other key reasons - cost, precedent and program stability.

Cost: While we feel an obligation to educate our customers about historic rates, we believe that the long-term price tag of extending this benefit to all borrowers all the time must be considered. For example, during the first three-quarters of the 2002–2003 academic year, about $28 billion in FFELP loans were consolidated. These new consolidation loans will cost the federal government an additional $4 billion over the life of the loans. An additional one-time consolidation by all loan holders who consolidated prior to this month's reset, and they all have rates above the current ones, would cost the government more than $15 billion as interest rates return to historic averages. Even at more moderate interest rate levels, the cost of these consolidation subsidies will dwarf the cost of the underlying FFEL program.

By not addressing the issues in the current consolidation program and/or by permitting reconsolidation, Congress is providing a costly new benefit—in the form of new repayment subsidies—to borrowers who have already completed their education and are in the workforce. It makes little sense to heavily needs-test the financial aid program on the front-end and then confer deep back-end subsidies regardless of borrower need. It also invites questions of fairness for those borrowers who are not fortunate enough to take advantage of historically low rates today. Will these borrowers also be granted the ability to lock-in below-market interest rates as low at 2.82%? Consolidation could become the giant that swallowed the student loan program.

Precedent: Most lenders enter into hedging agreements and securitize their loans to raise funds for future loans. Recognizing that lenders have legally binding contracts as part of the student loan program, Congress has never significantly changed the terms of student loans retroactively. Permitting retroactive reconsolidation of loans that have been financed through securitization transactions would fundamentally alter contracts between loan providers and investors after the contracts were made. If Congress breaks the terms of existing contracts, a level of uncertainty will be introduced into the program and make the prospect of investor-driven litigation likely. Congress will be sending a clear message that loan terms could change at any future point. The cost of this uncertainty will have to be built into every future loan—Stafford as well as consolidation.

Program stability: Understanding loan securitization is critical to appreciating the challenges loan providers would face if Congress authorizes borrowers to reconsolidate their already consolidated loans. Loan securitization is the principal means of making private sector capital available for students and families to help them pay for college. After a student loan is made, most large loan providers finance their portfolios of student loans through asset securitization to free up capital and make more student loans to new students. The end result of these transactions is that more capital is available to make higher education possible for more students who need to borrow money to pursue higher education. The loan provider continues to maintain the customer relationship with borrowers and retains certain residual cash flows from securitization trusts. The stable terms and predictable loan performance of student loans enable lenders to pass on low funding costs to borrowers in the form of reductions in up-front fees and interest rates, as well as other benefits that save millions of borrowers hundreds of dollars each. Most importantly, securitization frees up funds for loans that ultimately make higher education possible for more students.

Lenders securitize student loans, and investors invest in securities backed by student loan assets, based upon the statutory terms of loans, including the prohibition on reconsolidation. If Congress were to retroactively change the contract terms of loans, investors would be faced with a level of risk that would be impossible to quantify. From Sallie Mae's perspective, such a change could also delay the Congressionally-mandated privatization of our Government–Sponsored Enterprise (GSE). Enacting a reconsolidation proposal would retroactively alter the terms of loan contracts, destabilize the securitization marketplace and shrink the amount of capital available to lenders in the future.

The Single Holder Rule

Under current law, a borrower whose FFELP loans are held by a single loan provider must initially request consolidation from that same provider. If their loan provider declines to provide a consolidation loan, or declines to provide a consolidation loan with an income-sensitive repayment schedule, they can apply for a consolidation loan from another loan provider. Borrowers with loans that are held by more than one loan provider may consolidate with any eligible loan provider. This provision, referred to as the "single holder rule," ensures that lenders" portfolios are not cherry-picked and protects "borrowers from mass marketing or selective marketing of consolidation loans." (Conf. Rept. 105–750)

Why does this matter? The financial aid community and Congress depend on us to provide capital, pay up-front fees, and pay for the technology network that processes loans and data within seconds. All of these investments are made by loan providers four years before the average student makes the first payment. As with reconsolidation, if a loan provider's student loan asset is subject to poaching by another lender, there will be little incentive for loan providers to invest in the financial aid delivery systems that directly benefit schools or lower the cost of borrowing for students. Without the single holder rule, lenders would be incented to be only in the consolidation business, not the student loan business.

Although some argue that the single holder rule should be repealed, Congress" concern that borrowers be protected from predatory telemarketing efforts, reflected

in the 1998 Conference Report, has turned out to be prophetic. A few companies and telemarketing firms that are involved in the loan consolidation market are aggressively urging Congress to dramatically restructure the student loan program. These companies engage in repeated mass solicitations of these prospects. Repealing the single holder rule is a solution in search of a problem. Any borrower who wants to consolidate their student loans today can do so. And since the interest rate is set by statute, all lenders offer the same rate. While this proposal is promoted as a consumer choice issue, FFELP borrowers exercise their consumer choices at the time they borrow their Stafford or PLUS loans. Elimination of the single holder rule could result in aggressive marketing by non-lenders to borrowers without full disclosure of the benefits and risks of consolidation.

What Congress SHOULD do about loan consolidation.

Late last year, Sallie Mae joined with the Consumer Bankers Association, the Education Finance Council, the Secondary Loan Servicing Alliance and the National Council of Higher Education Loan Programs and submitted several recommendations to this Committee about ways to strengthen the loan consolidation program as part of HEA reauthorization. I will quickly summarize these recommendations as they relate to the consolidation program. Again, a copy of our complete recommendations is attached to my testimony.

1. To ease borrower repayment, we recommend that Congress retain the standard 10-year repayment term and make a voluntary, tiered repayment term available to Stafford loan borrowers as an option. This could be modeled after consolidation loan repayment terms, which allow for more reasonable monthly payments. We also propose permitting loan providers to provide borrowers with more flexible graduated repayment schedules.
2. Borrowers should not be forced to guess the best time to make their consolidation decisions. Currently, borrowers who need payment relief offered by consolidation loans may receive high or low interest rates depending upon the year and interest rate environment in which they happen to elect to consolidate their loans. Ensuring that borrowers retain their original interest rate structure (fixed or variable) in consolidation would avoid this trap.
3. We recommend that Congress make borrower eligibility the same for Direct and FFELP loan consolidation loans by making only borrowers in grace or repayment eligible for Direct Consolidation Loans.
4. To ensure that borrowers fully understand the benefits and disadvantages of loan consolidation, Congress should require borrower counseling concerning loan consolidation.
5. We recommend that Congress retain the single holder rule to avoid mass marketing to borrowers and incent lenders to invest in the student loan program.

What Congress should NOT do about loan consolidation.

Congress has never retroactively significantly changed the terms of existing student loans. Any proposal that seeks to retroactively alter the terms of existing loan contracts must be rejected. Setting aside economics, changing the terms of pre-existing loans would telegraph a message of program instability. It raises more questions: What other terms will Congress change retroactively? How can loan providers make loans under the cloud that Congress could change the loan terms at any time or for any reason?

As you know, financial markets do not react well to instability. The net effect of instability in the financial markets is that the cost of capital goes up. Changing the terms of loans retroactively would seriously undermine long-term private investment in the FFELP and puts at risk the $250 billion in private-sector capital that has already been invested in financing the higher education of millions of borrowers.

If Congress chooses to provide relief to borrowers who have previously consolidated, it is critical that any solution to this matter be addressed outside of existing student loan contracts. In other words, if Congress determines that some consolidation borrowers should be relieved of their repayment obligations, the mechanism for providing this new subsidy should be payable to the borrower outside of the student loan contract.

Conclusion

America's student loan program is a remarkably successful public-private partnership that has helped make college possible for more than 50 million students. In evaluating the merits of changing the terms of this partnership, we believe that there are three fundamental questions that must be asked.

First, will the proposed change increase access to higher education?

Second, what is the cost to taxpayers of the proposed change?

Finally, will the proposed change strengthen the successful public-private partnership embodied by the federal student loan program?

We believe that the consolidation program is in need of fundamental reform and that any savings that result from such reform should be spent on improving access to all students. We oppose proposals that permit reconsolidation or repeal the single holder rule, as they not only fail to improve college access, but they seriously undermine future access by introducing substantial new long-term costs to the student loan program.

Thank you for the opportunity to talk with you today. I would be pleased to answer any questions you may have.

[Attachments to Ms. McCormack's statement have been retained in the Committee's official files.]

Chairman MCKEON. Thank you.

Mr. Morrow.

STATEMENT OF BARRY MORROW, CHIEF EXECUTIVE OFFICER, COLLEGIATE FUNDING SERVICES

Mr. MORROW. Mr. Chairman and members of the Committee, thank you for the opportunity to talk about a program that is critically important to helping America's college students manage the growing burden of student loan debt.

The average student today graduates with over $19,000 in student loan debt at a time when the job market is weak and cash-flow pressures are often severe. Consolidation allows these students to refinance their multiple loans into one new loan with a low fixed rate and a payment that often saves hundreds of dollars a month.

College affordability is a key issue in this reauthorization. Some allege that the consolidation program diverts Federal resources that would otherwise make college more affordable. Stop and think a moment. For the most part, students don't have to pay loans back while they're in school. The reality of college cost doesn't hit until the student leaves college and has to start making payments. That's when the bill for college comes due and consolidation makes that bill more affordable.

Some argue that consolidation has strayed from its original purpose which was to assist student borrowers having multiple lenders. However, that was an era of much smaller debt. As college costs and student loan debt have increased dramatically for the past few years, consolidation has become a vital tool in managing these debt levels.

I spent most of my career in this industry. As a senior officer of Sallie Mae and then at the Department of Education and now as the CEO of a full service provider of student loans, and also as a father of three college graduates. As a result, I have reviewed the debate over consolidation loans from a variety of perspectives.

It is my belief that the debate over consolidation loans comes down to whether or not this Congress is going to put the best interest of students and their families ahead of a desire by big financial institutions to protect profits.

Most big financial institutions don't like consolidation loans because they're less profitable. Lenders have to pay the Federal Government a half a percent origination fee on each loan made as well as an annual fee of 1.05 percent on each loan each year. The result of these fees is that since fiscal year 1995, lenders have paid to the

Federal Government a $1.3 billion surplus, a fee income in excess of subsidies.

Now it's true that the unusually low rates of today may lead to future costs. However, it is important to note it's for this particular group of loans only, that is, consolidation loans disbursed between July 1, 2002 and June 30, 2004.

The economic policy group from Ernst & Young is completing a study on the incremental cost of consolidation that we will provide to the Committee. According to the study, if you recognize this current group of loans as water over the dam in the sense that the pending reauthorization comes too late to impact them, and if you look ahead to the fiscal year 2005 to 2010 timeframe, between this reauthorization and the next, then, based on current CBO interest rate estimates, fixed rate consolidation rates made during that timeframe are estimated to create a further revenue surplus of $700 million.

Those who oppose consolidations, the consolidation program, offer two alleged solutions. One is an extended repayment term for the underlying loans that otherwise are subject to consolidation. The problem with this is that these extended term loans would deprive the Federal Government of billions of dollars of fee revenue generated by the consolidation program today. It's a bad deal for the taxpayer.

The other alleged solution is to make all new consolidation loans variable rate instead of fixed rate. However, many of you will recall that during the 2002 interest rate fix legislation came out of this Committee which decided that as of 2006, all new student loans will move to a fixed rate. Students clearly prefer the certainty and simplicity of a fixed rate.

In closing, I'll briefly mention two final topics. The so-called single lender rule provides that if a student wishing to consolidate has all their student loans with the same lender, then that student must utilize that lender to consolidate even if better rates, terms and service are available elsewhere. This Committee had, in the Chairman's mark of the 1998 reauthorization, a full repeal of this ruling.

We are merely asking you to do what you did in the House during the last reauthorization, which is to repeal this anti-consumer rule.

The topic of reconsolidation. If the law were changed to permit reconsolidation, it would be costly to our company and to all student loan lenders. We'd be turning higher rate loans into lower rate loans. But student loan borrowers clearly want the ability to reconsolidate and if Congress can work out the budget-scoring challenges of reconsolidation, we support whatever is best for student loan borrowers and their families, even if our revenues take a hit in the process.

To make the burden of growing student loan debt more affordable for America's college graduates, I hope you will continue support of a vibrant student loan consolidation program.

Thank you.

[The prepared statement of Mr. Morrow follows:]

Statement of Barry Morrow, CEO, Collegiate Funding Services

Summary:

- Consolidation is a key tool to help student loan borrowers manage the growing burden of student loan debt. Most students don't have student loan payments in college. The real affordability crisis hits after college, when the payments begin.
- Consolidation is not a program that benefits the affluent. Nearly 20% of consolidators are nurses and teachers.
- Big financial institutions don't like consolidation loans because they are less profitable.
- The consolidation program has generated a surplus to the federal treasury of $1.3 billion between fiscal year '95-'02. CBO estimates an additional $1 billion surplus for fiscal year '03-'04.
- Estimates of future subsidy costs of consolidation are highly interest-rate sensitive, and thus, are probably exaggerated. They are based on materially higher future interest rates, contrary to the low rate outlook of the Federal Reserve.
- Extended repayment of Stafford loans would be very costly because it would deprive the federal government of billions in lender-paid fee revenue.
- Student borrowers prefer the simplicity and certainty of a fixed interest rate.
- Congress should require enhanced consumer disclosure language and unbiased borrower counseling for consolidation loans.
- The single lender rule keeps student borrowers from comparison shopping for the best rates and terms when consolidating. It should be repealed.

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to talk about a program that is critically important to helping America's college students manage the growing burden of student loan debt. The average student today graduates with $19,000 in student loan debt at a time when the job market is weak and cash flow pressures are often severe. Consolidation allows these students to refinance their multiple loans into one new loan with a low fixed rate and a monthly payment that often saves hundreds of dollars a month in cash outflow.

College affordability is a key issue in this Reauthorization. Some allege that consolidation diverts federal resources that would otherwise make college more affordable. But stop and think a moment. Although the perception of affordability is a barrier to access for those students concerned about incurring loan debt, for the most part students don't have loan repayment burdens in college. The reality of affordability doesn't hit until the student leaves college and has to start making loan payments. That's when the bill for college really comes due—and consolidation makes that bill more affordable. Unfortunately, according to a recent Harris survey, 53% of graduating college seniors are unaware of the consolidation program.

Some argue that the consolidation program has strayed from its original purpose, but what in the student loan industry hasn't? Sallie Mae, once prohibited by statute from originating student loans, now competes vigorously with the lenders it was originally created to serve. Wall Street securitizations of student loans have largely replaced the need for taxpayer-supported non-profit state secondary markets, although the latter continue to persist. Guaranty agencies have diversified into loan origination and servicing. And the Department of Education's Direct Loan program vigorously competes in the marketplace. Yes, the consolidation program has changed—- like many of the other changes, it has become better for consumers.

The original purpose of consolidation was to assist student borrowers having multiple lenders. However, that was in an era of much smaller debt levels. For example, median undergraduate debt has skyrocketed about 80% since just 1997, and is now about $19,000. As college costs and student loan debt have climbed dramatically in the past few years, consolidation has become a vital tool to make those high debt levels more affordable—and post-graduation affordability has become a major problem. A Roper survey last year found that a significant percentage of graduates had to pursue a career choice other than the one they preferred in order to make their loan payments. Recent articles in the Washington Post and the New York Times have reported on a finding in a survey by the Partnership for Public Service that two thirds of law school graduates would not consider public-interest or government jobs because their income would be too low to make their student loan payments.

It should also be noted that consolidation provides a potent default prevention tool, as described in a study entitled "Factors Affecting the Probability of Default", published in the Journal of Student Financial Aid, Vol. 32, No.2 (2002.)

The Congress realized the need to make loans more affordable during the 1998 Reauthorization of the Higher Education Act. It did so by making consolidation

loans more readily available and opening up the marketplace to far greater competition. This has provided significant benefit to the more than one million student loan borrowers just last year.

Opponents of the consolidation loan program claim that the program benefits primarily doctors, lawyers, and other high-income professionals. However, data we are providing to the Committee shows quite the opposite. According to a large study done by Experian (the credit reporting agency), less than 4% of consolidators are doctors and lawyers—and nearly 20% are nurses and teachers. Their average age is only 27. This is not a program that favors the affluent.

I've spent most of my career in this industry. Before joining Collegiate Funding Services, I was a senior manager in the Office of Student Financial Assistance at the U.S. Department of Education. Prior to that, I was a senior officer at Sallie Mae for nearly 20 years with responsibility for its then 4000 employees handling loan origination and customer service operations. In fact, when Sallie Mae temporarily withdrew from the consolidation program a few years ago in protest over the federal imposition of new lender-paid fees on consolidation, I was involved in the shutdown. As a result, I've viewed the debate over consolidation loans from a variety of perspectives. It is my belief that the debate over consolidation loans comes down to whether or not Congress is going to put the best interests of students and their families ahead of the desire by big financial institutions to protect their profits.

Most big financial institutions don't like consolidation loans because they're less profitable. Lenders have to pay the federal government a half-percent origination fee on each loan made, as well as an annual loan rebate fee of 1.05% each year on each consolidation loan in the lender's portfolio. The result of all those fees is that, since fiscal year 1995 (as far back as we could obtain data), the federal government has received a $1.3 billion surplus of fee income in excess of subsidies. The CBO estimates that for fiscal years '03-'04, consolidation loan revenues will provide a further surplus of $1 billion. By the time of the completion of this reauthorization, more than $2 billion in fees will have inured to the Federal taxpayer that would not have been paid had the loans not been consolidated.

Now, it's true that the unusually low interest rates that have been available for the last year or so will likely lead to future net subsidy costs. However, it is for this particular group of loans only (loans disbursed between July 1, 2002 and June 30, 2004). Opponents of consolidation like to use examples such as a $75,000 loan that lives for 30 years in order to show how much interest subsidy risk exists for the government. However, the reality is that the average consolidation loan is about $25,000 and usually is paid off before its maturity, typically in about 12 years. It should also be noted that many of the speculative estimates of the future cost of the consolidation program assume materially higher interest rates in the future. This runs counter to the Federal Reserve's statements that interest rates are expected to remain relatively low for a considerable period of time.

The economic policy group from Ernst & Young, LLP, is completing a study on the incremental cost of consolidation that we will be providing to the Committee. According to Ernst & Young, if you recognize the current group of unusually low rate loans as "water over the dam" in the sense that the pending Reauthorization comes too late to impact them, and if you look ahead to the fiscal year 2005–2010 time frame between this Reauthorization and the next, then, based on current CBO interest rate assumptions, fixed-rate consolidation loans originated during that time frame are estimated to create a further incremental revenue surplus to the federal government of approximately $700 million.

Those who oppose consolidation offer two alleged solutions to their exaggerated claims of cost to the federal government. One is an extended repayment term for the underlying loans that otherwise are subject to consolidation. Big financial institutions like this concept because it would mean fewer consolidation loans, which translates into bigger profits. The problem with this is that extended-term Stafford loans would deprive the federal government of billions of dollars of fee revenue generated by consolidation. It's a bad deal for the taxpayer.

Extended repayment also does not allow consumers who are dissatisfied with the service their current holders are providing to consolidate and obtain better service with another lender. Recently, a major holder of student loans admitted it had improperly billed 800,000 of its customers, requiring increases in payment amounts often exceeding $100 per month. Student loan borrowers should have a way to escape service problems of this kind; consolidation provides it—unless the problematic service provider holds all of a borrower's loans.

The other alleged solution offered by consolidation's opponents is to make all new consolidation loans variable rate instead of fixed rate. However, many of you will recall that during the so-called "2002 interest rate fix" legislation which came out

of this Committee, it was decided that as of 2006 all new student loans will move to a fixed rate. Students clearly prefer the certainty and simplicity of a fixed rate.

Another contentious topic is the so-called "single lender rule." It provides that if a student wishing to consolidate has all their student loans with the same lender, then the student must utilize that lender to consolidate—even if better rates, terms, and service are available elsewhere. On the other hand, if a student's underlying Stafford loans are owned by multiple lenders, then the student is free to comparison-shop for the best deal.

Congress recently spoke to this issue in the Conference Report accompanying the Omnibus Appropriations Act for FY 2003 (page 1141):

> "The conferees continue to be concerned about issues within the consolidation loan program. The conferees are aware that some borrowers would like to see the current law changed to allow for consolidation with any lender or holder, regardless of how many lenders with whom the borrower has loans. The conferees are concerned that without change to the current law governing consolidation loans, some borrowers may not be permitted to consolidate their loans with any lender they choose. The leaders of the authorizing committees have expressed a desire to address this and other issues during the reauthorization of the Higher Education Act so as to address the Consolidation Loan Program as a whole. The conferees urge those committees to ensure borrowers have the best options available to them in order to manage their student loan obligations."

Additionally, Congressman Joe Wilson, a member of this Committee, said during the floor debate on the Teacher's Bill:

> "While it would be great if no teacher would have student loans, for those who do have debt we need to make sure every student loan borrower has a REAL opportunity to consolidate their loans. Later during the reauthorization of a different part of the Higher Education Act we will need to make sure that we repeal the single holder rule. It will be part of my commitment to teachers everywhere that they can have the benefit of competition from the more than one thousand lenders in the program when they consolidate their loans and, thus allow them to further reduce their debt burden by taking advantage of historically low fixed interest rates."

Big financial institutions—wanting to protect their loan portfolios from competition—argue that repeal of the single lender rule would cause lenders to exit the business and have a negative impact on access to loan capital. This is an empty threat. Competition for student loan business is more vigorous than it's ever been...just ask any college financial aid director.

In an article in the May, 2003 edition of the Greentree Gazette, Paul Sheldon, Managing Director at Salomon Smith Barney's Education Finance Group, supported the view that student loan capital is unthreatened. He wrote: "There appears to be no practical limit to the appetite of lenders to make student loans. There is very aggressive competition for loans among huge financial institutions. There is growth in smaller size specialty companies. And a handful of new entrants are growing very rapidly. The supply of funds for growing loan volume is ample."

This Committee had, in the Chairman's mark of the 1998 Reauthorization, a full repeal of the single lender rule (which is a budget-neutral initiative.) We are merely asking you to do what you did in the House during the last Reauthorization, which is to repeal this anti-consumer rule. Imagine a federal law that restricted the ability of homeowners to comparison-shop for the best deal when refinancing their mortgage. Make sense? Of course not, and neither does the single lender rule. It is time for Congress to repeal this special interest, anti-consumer piece of legislation.

In addition to repealing the single lender rule, we urge the Committee to require enhanced consumer disclosure language and borrower counseling for consolidation loans. Although most of the companies offering consolidation loans adhere to high standards, regrettably there are some fly-by-nights that tarnish the reputations of everyone. CFS is concerned about that and has joined with other leading consolidation lenders to form the Student Aid Integrity Coalition. Members of the Coalition are substantial companies, typically being among the Top 50 holders of FFEL loans in the program, with multi-billion dollar student loan portfolios, AAA-rated Wall Street securitizations, hundreds of employees, Advisory Boards of financial aid directors from top colleges, and a substantial investment in the long term success of the FFEL program. In consultation with financial aid administrators and student groups, the Coalition has developed a list of pro-consumer best operating practices covering such things as no deceptive marketing practices, required employee training, borrower counseling, strict adherence to do-not-call lists, etc. Members of the Coalition agree to adhere to these best practices as a condition of membership. Like other Members of our Coalition, CFS does periodic customer satisfaction surveys.

Our last survey showed that over 95% of our customers would do business with us again and would refer us to a friend. We take our commitment to our customers very seriously.

In closing, I'll comment on the topic of re-consolidation. The Higher Education Act currently provides that once a student consolidates, they cannot re-consolidate. If the law were changed to permit re-consolidation, it would be costly to our company—and to all student loan lenders—because we'd be turning higher interest rate loans into lower rate loans. But, student loan borrowers clearly want the ability to re-consolidate and if Congress can work out the budget-scoring challenges of re-consolidation, we support whatever is best for student loan borrowers—even if our revenues take a hit in the process.

To make the growing burden of student loan debt more affordable for America's students, I hope you will continue to support a vibrant student loan consolidation program.

Thank you again for the opportunity to testify today.

Chairman MCKEON. Thank you. Mr. Wozniak.

STATEMENT OF PAUL W. WOZNIAK, MANAGING DIRECTOR, UBS FINANCIAL SERVICES, INC.

Mr. WOZNIAK. Thank you, Chairman McKeon, Ranking Member Kildee, members of the Subcommittee.

I am Paul Wozniak. I am the head of the largest student loan group involved in financing higher education and student loans in the country. What I was asked to describe for this Subcommittee is the manner in which education loans, and specifically consolidation loans, are financed and to address market issues that may arise as a result of permitting such loans to be reconsolidated.

Education loans are held by a variety of entities, including by for-profit, not-for-profit and state agencies. During the past 18 months, some $58 billion of long-term securities were issued by these entities to finance postsecondary education loans, primarily FFELP loans. Approximately 30 percent of this amount has been consolidation loans. Additional capital was provided to a lesser extent to this sector by lenders through other internal sources of funds.

The securities issued take many forms, but there are many common themes. One, they are issued as asset-backed securities, basically meaning that the loans themselves are used to pay off the debt or other type of financing; two, they are structured with a variety of complexity, depending upon how complex the loan portfolio is.

And in one little point of note, always talk about Stafford, Plus and consolidation loans as three basic loans. There are so many permutations of those types of loans that our models actually model about 150 different variants to what we have outstanding there.

Three, they are structured to meet strict rating agency stress tests to ensure that we have an investment grade rating to be able to sell to investors, and four, the programs are generally designed to meet investor preferences because that's going to get you the most efficient cost of funds.

The securities are distributed globally to investors and include securities including things called floating rate notes, auction rate notes, reset notes and fixed rate bonds. Each of these are just different types of financing mechanisms and have really long matu-

rities, some of them beyond 30 years, to accommodate very long lives that the loans could become in this student loan program.

Many programs also incorporate interest rate swaps or other types of derivatives and all those loans are usually put into a trust that's used again to pay down to the bondholder.

The purpose of using derivatives or interest rate swaps is actually one to allow hedging mechanisms to be able to match your cost of funds. You want to be able to match your borrowing costs to your asset that you're trying to finance and make sure that you've got a revenue stream that's similar and, two, there's also a reason that you may want to convert what one investor preference may be by issuing to that investor's preference and then, indeed, using a synthetic mechanism to allow you to finance better.

An example of this is in the U.S. market, floating rate notes are a very attractive financing vehicle but it's not easy to find a lot of U.S. dollar assets that are willing to be invested in a long-term mode. However, there are other currencies where people like to have variable rate investments in that manner and what is done is basically using these interest rate swaps, and again, they're contracts under the trust, to basically put together to match what the investor wants with the portfolio that the issuer wants to be able to—the lender wants to be able to finance.

With this as background, there is one thing that lenders and investors value most and that's predictability. The greater the predictability, the more efficient the pricing of the debt will be. The more efficient the pricing of the debt, the better able the lender will be to offer borrowers the most beneficial terms and, ostensibly, those lenders offering the best terms and service to students will achieve a growing share of the market.

Investors that have invested in student loan backed securities have been drawn to the sector by the relative predictability of the cash-flow repayment stream despite the many unique features inherent in the FFELP program. Floating rate note investors, in particular, carefully analyze the speed at which they expect a portfolio of loans to repay.

Significant variances from expectation cause investors to reassess the risk or value of an investment. Identifiable market developments may cause an investor to reevaluate the model. Systematic risk, such as legislative risk, may be viewed with more caution, as it is less predictable and not market driven.

A loan refinancing option that gives borrowers a second bite at the apple is something that most investors could not have contemplated in assessing the average life of their investment. The original consolidation option was generally viewed as a mechanism that permitted those with multiple loans to combine them into a single loan thereby resulting in a single borrower repayment, or by those borrowers with large balances to achieve a more manageable monthly payment through extended repayment.

Reconsolidation, on the other hand, will only target certain loans, as currently proposed, most attractive to borrowers that may have consolidated several years ago at a much higher rate, those having the greatest value within the outstanding trusts. So those would be the most likely to be reconsolidated.

It's safe to say that as a result, investors in all types of student loan backed securities will be unambiguously less secure, on a relative basis, in the event of reconsolidation than they would absent a reconsolidation option. The magnitude of this decreased security may only be assessed on a trust-by-trust basis, depending on the portfolio and what type of contracts may have been entered into.

One of the things that investors—investors have already signed on in both the floating rate and the fixed rate investors, they've already agreed to accept a certain yield spread or interest rate on those securities for the life of the offering. It's a risk that they will bear as the market adjusts to new information.

Investor memories are quite long and increased prepayment speeds and the potential loss of favorably performing collateral, potentially creating a negative selection bias for the portfolio, will invariably be factored into future investors evaluations of the sector. Presumably, investors would also increase the weight that they place on the evaluation of legislative risk to the extent that it could be measured.

As there is a large foreign investor base, especially in floating rate notes, their ability to assess or manage this potential risk is somewhat diminished, therefore it is difficult to assess a magnitude to any investor response.

Reconsolidation will also have an impact on the Direct Loan portfolio. As the government continues to look at certain options to manage its own portfolio, a reconsolidation option will diminish the value to the government and will be able to realize—that they'll be able to realize on any loan sales or securitizations of its own.

The implications of reconsolidation of consolidation loans are subtle, to be sure. It's important to weigh the goals and benefits of any new options against the goals and benefits of the entire FFELP program. The ability of lenders to continue to raise capital on the most efficient basis possible should be one of the criteria included in this evaluation, because this has been one of the driving factors in providing borrowers the benefits and services they've come to expect.

I thank you for the opportunity to address you this afternoon.

[The statement of Mr. Wozniak Follows:]

Statement of Paul W. Wozniak, Managing Director, UBS Financial Services Inc.

Good Morning. I am Paul Wozniak, a Managing Director and Group Manager of UBS Financial Services Inc.'s Education Loan Group. The Group is the largest of its kind on Wall Street, and we are mandated to coordinate all education loan related finance activities in the Asset–Backed Finance, Taxable Fixed Income and Municipal Securities Departments. Last year my group managed $12.5 billion of education loan financing activities. I am currently in my 22nd year of financing postsecondary education loans.

I was asked to describe for the Subcommittee the manner in which education loans, and specifically consolidation loans, are financed and to address market issues that may arise as a result of permitting such loans to be reconsolidated.

Education loans are held by a variety of entities including for-profit and not-for-profit corporations and state agencies. During the past 18 months, some $58 billion of long-term securities were issued by these entities to finance postsecondary education loans, primarily FFELP loans. Additional capital was provided to a lesser extent to this sector by lenders through other internal sources of funds.

The securities issued took many forms, but generally reflected common themes; (i) they were asset-backed (meaning secured by the loans themselves) securitizations or debt financings, (ii) they were structured vehicles of various complexity, (iii) they

were structured to meet strict rating agency stress cases to achieve investment grade ratings and (iv) they were designed to meet investors" preferences. Further, it is essential to the rating agencies rating opinion that asset securitizations are issued via a bankruptcy remote trust or entity.

The securities were distributed globally to investors and included such securities types as floating rate notes, auction rate notes, reset notes and fixed rate bonds. Virtually all these securities have very long dated maturities. To achieve the most efficient structures, many programs incorporated derivative products into the trust. The purpose of these instruments is generally twofold: First, to provide asset-liability management or match funding for the assets, and second, to allow an issuer to access one market that may be preferred by investors, and synthetically converting the risk of the obligation to something more useful to the issuer.

For example, while the US dollar floating rate note market ("FRN") is an excellent funding vehicle for FFELP loans, investor demand is thin for longer maturities, especially maturities that would help securitize the longer cash flows of consolidation loans. However, there is longer term investor interest in Euro denominated floating rate notes. Hence, a derivative product can be employed to convert Euro currency and rate risk to US dollar rates in a less expensive manner than could otherwise be done directly with US dollar investors around the world.

With this as background, there is one thing that lenders and investors value most and that is predictability. The greater the predictability, the more efficient the pricing of the debt will be. The more efficient the pricing of the debt, the better able the lender will be to offer borrowers the most beneficial terms, and ostensibly, those lenders offering the best terms and service to students will achieve a growing share of the market. Investors that have invested in student loan backed securities, have been drawn to the sector by the relative predictability of cash flow repayment despite the many unique features inherent in the FFEL program. FRN investors, in particular, carefully analyze the speed at which they expect a portfolio of loans to repay. Significant variances from expectation cause investors to reassess the risk or value of an investment. Identifiable market developments may cause an investor to reevaluate its model. Systematic risk, such as legislative risk, may be viewed with more caution, as it is less predictable or market driven.

A loan refinancing option that gives some borrowers a second bite at the apple is something that most investors could have not contemplated in assessing the average life of their investment. The consolidation option was generally viewed as a mechanism that permitted those with multiple loans to combine them into a single loan thereby resulting in a single borrower repayment, or by those borrowers with large balances to achieve a more manageable monthly payment through extended repayment. Reconsolidation, on the other hand, will target only certain loans (as currently proposed, most attractive to borrowers that may have consolidated several years ago) having the greatest value in outstanding trusts. It is safe to say that as a result, investors in all types of student loan backed securities will be unambiguously less secure than they would be absent a reconsolidation option. The magnitude of this decreased security may only be assessed on a trust-by-trust review, and for FRN and fixed rate investors who have already agreed to accept a certain yield spread or interest rate on their securities for the life of the offering, it is a risk they will bear as the market adjusts.

Increased prepayment speeds and the potential loss of favorably performing collateral (potentially creating a negative selection bias for a portfolio) will invariably be factored into future investor evaluations of the sector. Presumably, investors may also increase the weight they place on an evaluation of legislative risk to the extent that it could be measured. As there is a large foreign investor base, especially in FRNs, their ability to assess or manage this potential risk is somewhat diminished. Therefore, it is difficult to assess a magnitude to any investor response.

Reconsolidation will also have an impact on the Direct Loan portfolio. As the government continues to look at certain options to manage its portfolio, a reconsolidation option will diminish the value the government will be able to realize on any loan sales or securitizations of its own.

The implications of the reconsolidation of consolidation loans are subtle to be sure. It is important to weigh the goals and benefits of any new options against the goals and benefits of the entire FFEL program. The ability of lenders to continue to raise capital on the most efficient basis possible should be one of the criteria included in this evaluation, because this has been one of the driving factors in providing borrowers the benefits and services they have so come to expect.

I thank you for your time.

Chairman MCKEON. Thank you very much. Now, this is a subject we've really been grappling with here on the Hill and in the Committee and I talk to people and I get different responses to different questions or I get different responses to the same question. And I'm happy to have all of you here. We have people from both sides of the issue, we have people that are somewhat objective on the issue.

And what I would like to find out, there was a question asked of the previous panel, is there any cost to the Federal Government for refinancing or consolidating loans. I think the answer came out kind of—was kind of nebulous, kind of no cost, or if there was a cost it would be recouped in other ways, taxes or something over a long period of time.

I would like to hear from you, is there a cost to refinancing or consolidating loans.

Mr. MARTIN. Mr. Chairman, yes, there is a cost. I mean, these are subsidized loans and that's what makes them unique. They're not the same—we've heard a lot of discussion today from people, well-meaning, talking about differences between products like home mortgages or automobiles or whatever, but those are not things that carry the same kind of subsidies and structure the way student loans are.

If the interest rates go back up, and we assume that they will because they're cyclical, then obviously there will be a cost on those assets with student rates being set, of what is the difference of paying that subsidy for the holder of that loan. And those are going to be costs that are going to have to be absorbed, just as we pay now on the regular loan program a special allowance cost on those loans.

The same thing is going to be true on these except we're dealing with unusually low interest rates, so it's going to be even more, depending on where that upper rate cap is set. So there is going to be a cost and my concern is not that I'm not sensitive or our association is not sensitive to people that are out of school that have a lot of debt. In fact, we have a lot of our proposals under the reauthorization to try to work on extending repayment terms, providing other kinds of benefits for students who are borrowers, even changing some of the benefits around so that we target them more successfully upon the most needy to try to keep indebtedness down.

But under this issue of loan consolidation, my concern is knowing that we have limited dollars, the question is should we spend those dollars now upon individuals who have received their education, who have been amply assisted, who had the benefit of in-school interest, have had their grace periods and so on, that are out in our society that are going to be successful—and not that I don't want to help them, but if I don't have enough dollars, is it better to use those dollars to come back over here to this new influx of students that we've got coming in that are very, very needy and we know the with costs going up—of having monies to assist those students so that they're going to have the same opportunity to get their education?

And that is—if we had unlimited funds, I would—might be one of the people who would say yes, let's see what—if we can't spend some more of this, because there is a great return on people to our society that have an education in terms of the amount that they're

going to pay in taxes, the contributions they make to our society, living healthier lives, participating more in civic governance, but the reality is we have a finite amount of dollars and I do not want to deny upcoming students the opportunity to get that education simply by providing continued subsidies to those that have already benefited.

Chairman MCKEON. Ms. McCormack.

Ms. MCCORMACK. Yes. Mr. Martin has certainly very eloquently pointed out that there is, one, a huge cost, and two, it would shift dollars from the front end of the program and providing access to the back end.

As I indicated in my testimony, we at Sallie Mae believe that cost is well in excess of $15 billion just for a single reconsolidation and would be substantially higher if borrowers were allowed to reconsolidate over and over again, particularly because interest rates may be going down even further over the next year.

So yes, there is a cost and it's definitely shifting dollars to graduates as opposed to having dollars available to help with access at the front end.

Chairman MCKEON. Mr. Morrow.

Mr. MORROW. Yes. I guess I'll be the lone wolf on this one. We talked about investments earlier in the first panel. If you look at the consolidation program and the student loan program as an investment, much like the stock market, prior to 1999 you bought stocks, you probably did pretty well. If you bought in 1999, you probably didn't do very well. Today, prices are back down.

Consolidation program is the same way. Between '95 and projected for 2004 for loans originated in 2002 is a surplus to the government because of fees paid by lenders to the government. Between '02 and '04, maybe a negative because of the unusually low interest rate period. '05 to '02, if rates normalize, which everybody expects they will do, there's a surplus back to the government.

This is a fairly simple issue to understand and I don't get the—why there's so much confusion about it. So if you look at the investment over the long haul and your broker always tells you with stocks, stay in for 10 years, stay in for 20 years. Much the same way with this investment.

Chairman MCKEON. Mr. Wozniak.

Mr. WOZNIAK. I guess if someone were giving me the task to do that computation—and I'm not volunteering for that—it would be somewhat akin to someone looking at a mortgage and saying, gee, should I go with the 5 percent mortgage with the changes every 3 years or the 6 percent locked in over the term? Which is going to be the better option?

And in many regards, because of the mechanics of the way that the consolidation program works and the various fees and interest rate assumptions, it's a very difficult fact to just say the answer is six. It's a very difficult assessment.

Mr. MORROW. Let me just add to what Paul said. It's difficult going forward because of the rate assumptions and you can play with rate assumptions in the out years and get the answer you want to get. But if you deal with facts, look at the facts, '95 to 2002, those loans that were consolidated generated a surplus to the government.

So if you deal with facts and not speculation about future interest rate possibilities, I think the facts speak for themselves.

Ms. MCCORMACK. I would like to correct Mr. Morrow's statement. Between that time period that he stated, approximately $1.3 million was ret—billion dollars was returned to the Federal Government but the cost was actually higher than that to the government for the loan program, so that's actually an incorrect statement in terms of the net impact.

Mr. MORROW. And I'll disagree with you on that comment. The 1.3 was net of subsidies.

Chairman MCKEON. Here's where I—this is a problem. This we deal with constantly. I would like both of you—or all four—all five of you to address that question in writing, if you could, and we'll get back to you and follow up on that because I'm really grappling with this, OK?

Ms. MCCORMACK. We would be happy to do that.

Chairman MCKEON. Thank you. Mr. Kildee.

Mr. KILDEE. Thank you, Mr. Chairman. Mr. Wozniak, in going over your testimony, you seem to close the door totally on reconsolidation. Am I reading your testimony right?

Mr. WOZNIAK. That's correct. From a standpoint, again, there are issues with regard to securities, again, that investors have certain preferences but from the standpoint of the most efficient market, it would be to maintain the status quo because that's the best. From the standpoint of the contractual issues, those will be some type of difficulties that may have to be addressed as well because there were certain assumptions as to how quickly some of those loans would pay down.

With regard to consolidating a loan and what it does going forward on changing the speeds, while that will change the cost of capital it may increase the cost of capital. It certainly would probably be more likely to increase the cost of capital to lenders rather than decrease it. That would be a correct reading.

Mr. KILDEE. Thank you very much. Mr. Morrow, your testimony mentions your support for elimination of the single lender rule. Why is this important to the competition between consolidators for borrowers and how is repeal going to benefit the student in the loan industry?

Mr. MORROW. Well, I'm not sure it's just the consolidators at issue here. The real reason, to me, behind the repeal of the single lender rule is competition. It's simply put, and I think Congressman Regula mentioned that in his testimony, that competition always is in the best interest of the consumer.

And by having an 18-year-old freshman have basically a loan provider chosen for them as opposed to free choice and then having to be locked into that situation irrespective of innovations that bring better price, better services, whatever, to have that person locked in for 10 years, even not speaking—not consolidation but just for 10 years, that lender seems to be kind of completely opposite consumer choice and what this country is about in terms of the capital markets and competition.

Mr. KILDEE. And it will help the student and will not drive out a healthy lender?

Mr. MORROW. Well, let me put it this way. When we started this back in 1998, people told us you couldn't offer discounts on these loans because you couldn't make money. We did. Did we make as much money as we could have? No, but we made money by offering discounts on these consolidation loans.

I work with three of the largest—five largest lenders in the program. They're very anxious to get these loans so I don't see a destabilization issue at all. I don't know where that comes from.

Mr. KILDEE. Thank you very much. Ms. Wasserman, your testimony mentions the need to do away with the origination fees. How much will elimination of these fees benefit the average student in terms of lower monthly payments or less interest paid over the life of the loan?

Ms. WASSERMAN. In terms of the exact numbers, we can get that to you but the key is these are important in reducing monthly payments but also in just sort of that students should not be paying interest on money that they don't ever receive and they're paying interest on the full amount of the loan, including these fees that they pay right away.

So just in terms of fairness, these fees should be removed. And I think that—I mean, this goes to sort of— I think the big question here that Chairman McKeon was just asking in terms of will consolidation have costs to the government, will consolidation, reconsolidation have costs.

I think for us it's about saying that that should not be the debate. The debate should be we need to help students and access. While we prioritize grants, the Pell grant, for example, we also see the need for consolidation and reconsolidation because students are graduating with unmanageable levels of debt.

So if we are able to remove origination fees, if we are able to do loan forgiveness, if we are able to do these consolidation programs, it means that the students that are graduating are able to help the economy and they are able to choose jobs based on what they want to do, not their monthly payments.

So I think whatever small amount it does is important.

Mr. KILDEE. Dallas, you said if we had unlimited or significantly greater amount of money we could have the consolidation and we should return it to its original purpose. There's no question if we had more money we could do a lot more things around here. We probably in the last 2 years have voted for—last two and a half years voted for about $2 trillion worth of tax cuts. Now, if we had maybe made it 2 trillion minus 12 billion, which is the figure I get as a cost of this, the 12 billion would help, would it not?

Mr. MARTIN. It certainly would. I mean, I would like to see $12 billion out of the Pell grant program, Mr. Kildee. There's a lot of things we could do in education with $12 billion. It would be a big help.

Mr. KILDEE. If it had been a rule germane I would have offered an amendment to the tax bill, minus $12 billion to be used for this purpose here, but I think I would have been ruled out of order.

Mr. MARTIN. I think you probably would have, sir.

Mr. KILDEE. Thank you very much.

Mr. MARTIN. Let me just—I would like to add one thing, though. It goes back to the question that Rebecca was saying about the fees and we also are on record of eliminating the origination fees.

And I do think that this is an issue that I hope the Committee will look at because that is money that is taken away that students are not receiving in many cases up front and I realize that in some cases lenders or others are providing that so not all students are paying that, but that is a fee that eliminates the purchasing power of that loan in the beginning.

And, yeah, that was put in back when we were dealing with high interest rates in the early 1980's. It was actually part of the Budget Reconciliation Act of 1981. And we were dealing with 13, 14-point percent interest at that time on short-term monies and we put that in as a short-term fix for students, to assist—to preserve in-school interest subsidy.

And I would suggest in this interest environment it is time to revisit that issue because we are long past that and that is money that does not go to help students that really need that that are borrowing that comes back to the government.

Mr. KILDEE. I believe your memory is correct on that. That was the purpose when it was put in in the first place and things have significantly changed since then. Thank you very much.

Chairman MCKEON. Thank you. Mr. Burns.

Mr. BURNS. Thank you, Mr. Chairman. I appreciate the panel, I appreciate the diversity of your viewpoints.

Let's go back to the consolidation and reconsolidation issue which I do not have a fundamental problem with. I have a fundamental problem with the American taxpayers subsidizing that. If we have an issue with fixed rates versus variable rates, perhaps, Mr. Morrow, what is the problem with going with the consolidation, reconsolidation at No. 1 variable rates and, No. 2, if the student chooses to reconsolidate and renegotiate a rate that they have for their education, why would it not then become their option and their alternative to do that independently without the government subsidy? What's the problem with variable rates if we can't agree on what a fixed rate might need to be?

Mr. MORROW. At the basic policy level probably there is nothing wrong with variable rates. We are moving toward, as current legislation calls for, a fixed rate program in 2006 because—

Mr. BURNS. At 6.8 percent, but we don't know what 2006 is going to look like. It might be high, it might be low.

Mr. MORROW. There might be some discussion about how that fixed rate should be set; I'm not sure what the mechanisms were—

Mr. BURNS. Or perhaps whether a fixed rate—

Mr. MORROW [continuing]. Whether there should be. But I think the issue that's missed here often, and it gets back to Ms. Wasserman's point, just kind of like they say in politics, it's the economy. In student loans, it's the payments.

It's not the rate. Look back at 1999 and 1998, 2000, even before, people needed cash-flow relief. That's the issue here. The accessibility issue, to me, is once those loans come due we have to start making payments and we're seeing people, Ms. Wasserman—we've actually done a study; it's referenced in my written testimony—peo-

ple are making life choices because of the amount of student loan debt they have. That shouldn't be the case.

When I was with the Department of Education we made a trip up to the Harvard School of Business and Government. We were speaking with a young lady who had gone through a very successful academic career and had taken on a lot of loan debt, Harvard and elsewhere, and was worried because she wanted nothing more than to go to work for the government in public service.

And her comment—it wasn't to me, it was to Mr. Woods who then ran the office of student financial assistance—was, I can't afford to take a job in public service because my monthly payment on my student loans will be over $700 a month and no public service job pays that well.

That's not what education investment should be about, in my mind.

Mr. BURNS. Was that not a choice of the student to accept the burden of that high cost of that high quality education?

Mr. MORROW. I agree. It was—

Mr. BURNS. And if you look at the testimony that Ms. McCormack provides, well over 50 percent of the subsidies are going to students with in excess of $40,000 in debt. Again, that's a terrible burden and as you suggest, you know, I just had two sons who went through the education environment and fortunately, you know, they did not have to deal with significant debt.

I'm all in favor of a free market. I'm in favor of an opportunity for students to determine what is best for their financial situation. I think the challenge we face is finding a mechanism that will afford that and at the same time not burden the taxpayer and not penalize those new students who are coming into the system quite dramatically over the next decade and allow us to focus the subsidies of the Federal loan payment programs on those new entering students.

Again, I think we have to look at the fact that originally we had a fixed rate for a fixed term and now what we're doing is we're seeing an extension of that term to from 10 years to 20 years to 30 years in order to get the cash-flows that you suggest, and I understand that.

But what we have to recognize is if the student chooses to refinance, that's a good thing and I'm open to that. But at the same time I'm not sure the taxpayer should be subsidizing the refinance.

Mr. MORROW. Let me clarify. There's two separate issues. On the consolidation program, back to my comment about the stock market, I don't think there's a cost to the government on the basic consolidation program. I do believe, as I said in my oral, that there probably is a budget-scoring issue with refinancing and depending how that may or may not be solved, that's almost a separate issue.

I believe there are some probably inherent costs in doing that but I think if it's something we can do because of the fact that constituents are asking for it, we should look at it. But the basic consolidation program, if taken over a long period of time, not just a blip in time, I think is cost neutral to the government, in some cases as the Ernst & Young study will show, in writing, cost positive.

Mr. BURNS. If indeed it is cost neutral, then a variable option might be something we would want to consider.

Mr. MORROW. I would have to look at the analysis, but it could be.

Mr. BURNS. In closing, if a student has a loan and they complete their education and enter the marketplace and they become professionally employed, hopefully, and have a positive earnings environment, if after that scenario they then choose to refinance—in other words, first of all, I would accept the fact that under our current program we should continue to support it and enhance it.

But once they move beyond the educational environment and are into the marketplace, they are making that decision because of the direct benefit they will receive from a lower interest rate. And when that happens, I think that it is not reasonable to then ask the taxpayer to subsidize their position and again to ask the lending institutions to accept the risk of the variation in the interest rates.

And I think once of things we want to look at is once we get beyond the student graduation point and into the marketplace and into a position of beginning the repayment plan, that we then allow them to refinance but let that be a market-driven decision as opposed to a Federal Government program.

Thank you, Mr. Chairman.

Chairman MCKEON. Thank you. Mr. Tierney.

Mr. TIERNEY. Thank you. One thing that the market hasn't provided for us is an affordable higher education for all students and that's why the state governments and the Federal Government are involved in the first place. I mean, it just simply isn't happening.

So I think going back to some of the comments that were made earlier, what we're looking at here is we supposedly have made a Federal commitment to the importance of education in higher education and we talked earlier—Ralph Regula was very good about talking about what other countries do in terms of making that commitment despite our lofty rhetoric.

So if we really believe that more education is a good thing, then obviously we could obviate a lot of this discussion by, as Dr. Martin says, put more money into Pell grants. Then we wouldn't be talking about trying to make sure the kids on the other end have a right to reconsolidate and get a break.

So I wonder if we're not looking at this thing inside out, that is, somehow capture that money that we're talking about, put it at the front end and giving kids more money in Pell grants, even in work study monies, I mean, something to get them to lower the cost so that the burden they have in the long run really comes down.

I think that makes more sense to those of us who went through that way, those of us who have kids that recently went through that way. It just seems—you know, this whole debate is one that we ought to be having after we talk about funding appropriately Pell grants and getting kids into college that can afford it.

Once kids are into college and we have encouraged them to go to school and we think that's good for the productivity of the Nation to move in that direction, then—once you get out, you have a burden and it's not a question of this kid saying, you know, I've got a choice or anything like that. We want them in.

And the choice is now do we burden them so that they have to make a career or a life choice once they get out, like, I got into

school and I was a relatively poor kid, I didn't have a family to pay for it and couldn't pay for it myself so I took a loan but now I can't go into government service because I chose to have an education or I wanted to get to the level where I could do something good in education or I go into a public service law firm instead of a big fancy law firm that pays six numbers?

And there are needs in all these places and those are choices that kids ought to be able to make. So I just think we're doing it at the wrong end for one part and that we do have to do something about giving them the opportunity to refinance and consolidate on the other end.

And Dr. Martin, I think you're absolutely right about doing it on that end but I think—what I want to know is how would a student be injured—and I guess I want to set up a little bit of a debate between Dr. Martin and Mr. Morrow here because I think you both mentioned this earlier in your comments.

If I'm a student who just comes out with a lot of loan and I want to talk about consolidating, what harm to me, as a student, would there be in consolidation? What things ought we look out for? Dr. Martin?

Mr. MARTIN. Well, from a student's standpoint I don't see necessarily a downside although, depending on who you consolidate with, I will have to say, Mr. Tierney, that we have had a lot of anecdotal information that's come back to us from some people who are very aggressive marketeers and selling consolidated loans that they have not fully disclosed to students what the downside is by consolidating, in terms of giving up other benefits.

Many of these people do not tell students, for an example, when they consolidate their loans that they may lose certain cancellation benefits because of their prior loans that carried those, such as a Perkins loan or something else—

Mr. TIERNEY. So we have to make—

Mr. MARTIN. —so it's important that we do that. We at the institutions, when students make loans, do precounseling and we do exit counseling. But many times when the students are doing consolidated loans, they're taking it out after they're out of school and so they're not necessarily subject to the same counseling.

And so—and I'm not saying everybody in the industry does that. I don't want to be misstated because I think some people are very responsible but we have enough evidence that a lot of students are being misled in terms of, oh, we're going to do all these wonderful things for you, without them realizing what they're giving up.

Mr. TIERNEY. Thank you. Mr. Morrow?

Mr. MORROW. I actually agree with Dr. Martin on this one. To the student, there really is no harm as long as they're getting the right information. As with any business, you do have interlopers who might not provide the best quality of service and that true and it's been true in the basic student loan program.

There's been cases where people that shouldn't have been in were in. That's the primary job of the Department of Education to control that eligibility, which they have done with the major players in the business. They have come and looked at what we're doing.

To address this issue, though, we've taken it a step farther. We have teamed up, actually with Ms. Wasserman's organization and others, to form a non-profit industry benefit type of corporation called the Student Loan Integrity Coalition. That coalition, just like the Good Housekeeping stamp of approval, will have standards of conduct in terms of how you do business when dealing with education loans, everything from what rights may you give up, what are your rights, what are your options under various programs.

There are a number of things that you might give up and consolidation is not for everybody and I think the organization doing it has to walk the individual through the pros and cons and be very up-front about it.

Mr. TIERNEY. Thank you. Ms. McCormack, I've got just a few seconds left. What harm to entities like Sallie Mae, consolidation? What are your list of grievances to it? For you. Don't tell me about the taxpayers because we'll take care of them but what about Sallie Mae?

Ms. MCCORMACK. For just plain consolidation, we think it's a good benefit for consumers and for borrowers who are having a difficult time managing their debt, consolidation can be a very effective way to manage that debt.

However, reconsolidation is very problematic in terms of the student loan contracts that we have in place with our investors and in the asset securitizations that we do which we believe will—the cost will be substantially increased as a result of reconsolidation.

Mr. TIERNEY. Well, wouldn't you adjust those once reconsolidation became a factor? Wouldn't you then make the appropriate adjustments for that?

Ms. MCCORMACK. These are outstanding contracts that are already in place. We can't adjust them.

Mr. TIERNEY. But future ones you would?

Ms. MCCORMACK. In the future, if there were changes in the rules of the program we would adjust them.

Mr. TIERNEY. Fine. What else? Anything else?

Ms. MCCORMACK. The biggest issue, I think, with reconsolidation, and I think we would certainly do this as well, is it causes the investment to go from the front end of the program to the back end. If we are not assured that we can hold onto an asset that we've spent millions of dollars in developing technology and support to create access for students to be able to get the loans and to have cost effective loans on the front end, we would be in the position as any other market consolidator out there and we'd be investing our dollars on the consolidation piece of the business instead of the front end access piece of the business and we think that's bad public policy and we think that's bad for students and it will do nothing to put another student in college.

Mr. TIERNEY. You don't think somebody else will just step into that part of the market?

Ms. MCCORMACK. If the rules change, absolutely, people will go into the reconsolidation part of the market.

Mr. TIERNEY. But somebody would step back and take whatever part you think you're going to move into.

Ms. MCCORMACK. I would think that the economics would not be there anymore. You would be trying to make a loan that you had

no assurance that you'd be able to hold onto once the loan was made.

Mr. TIERNEY. Thank you.

Chairman MCKEON. We have time for another round. If you could bear with us for a little bit longer, this is a rare opportunity for us.

Mr. Wozniak, I think you said in response to a question the status quo is best. When you're trying to package financing deals to sell, the lenders would like to know that forever out into the future nothing is going to change, it would just continue on and that way, then, they could take everything into account before they make their investment?

Mr. WOZNIAK. From the front end investment side, yes, that would be on the lender side, and then on the investor side as well they, too, would be benefited by saying I know what to expect because we've been going through this process for some period of time, stability, just like the Tax Code as well as the Higher Education Act. It's good to have something that's stable for a period of time because that gives a much better opportunity for people to get their arms around everything.

I don't think there's any question that the number of investors in the student loan marketplace, if you look over the last couple of years where there has been relative stability and especially after the fixes to the interest rate issue that the Committee—Subcommittee did so well previously, that has made a number of—it's just been a doubling of the number of investors who have come into this marketplace, so that's a positive.

Changes, obviously, will reshift the marketplace and the question is how will people view it, how will they be affected. Very difficult to tell until everything is put into the final rubric but clearly there would be some that would drop out.

Chairman MCKEON. Depending on what changes are made.

Mr. WOZNIAK. Depending on what changes are made; absolutely. I mean, obviously there are changes that wouldn't have much implication. In that case, the investor doesn't have an issue.

But to the extent that there are significant changes that are made, that obviously would have a much more dramatic impact and, as I said, probably in certain cases it could actually—again, you have to look at it on a case by case basis to see if there were particular items.

I can't possibly know every financing out there, but certainly there would be certain parties who, on the assumption that they had a particular fixed rate, you have that, fixed rate, that's set, OK.

I'm supposed to act prudent. I'm going to do my assets and liabilities appropriate, yeah, I know some things will happen but I wasn't expecting that.

Chairman MCKEON. They don't have a problem with a variable rate or a fixed rate. Their question is more what it's going to be, just so it's not going to be changed from one to the other, back and forth, or if they have a contract especially they wouldn't want to change.

Mr. WOZNIAK. Right. Well, in the reconsolidation case, effectively, if I had $100 of assets and they were at a 6 percent rate and I

locked in my financing at 5 percent saying, well, you know, I'm supposed to be prudent, the rates might rise. I don't know what the rates are going to do but they might rise tomorrow so I'll lock this in and I'll lock it in for the average life of the loan portfolio based on my prior history, knowing how those loans will actually pay down.

Then what happens is effectively if all of a sudden a new option—because, of course, loans can be paid down. People have been refinancing their mortgages and taking the money—I mean, basically what they've been doing is taking money out of their homes. That's over $300 billion has come out of the mortgage market, actually an increase in the amount of debt, and basically been used to pay down debt and do other things.

So there has been some pay down but to basically put an option on that now says hey, I can take this out, is kind of like if you were a bond investor and you bought a 5-year bond that had no call provisions, you know, at 6 percent and 2 years into it somebody says hey, I'm going to call the bond because now I can.

If you were holding that security, you wouldn't feel good about it and effectively what that can do is it would change the—potentially the credit quality of that particular portfolio. But as to variable or any type of variable or fixed, how does that go forward? That is—ultimately the marketplace will be able to finance that knowing what the new loan looks like. It's just a question of what happened to the old loan, how that affects what the expectations are.

Chairman MCKEON. So student loans have been around long enough that the investors know that every 5 years there's a reauthorization process and we're going to look at these things, assuming no change is made in between. I remember when we did the last reauthorization in '98, one of the big debates, one of the big concerns was the rate.

Remember the debate we had on setting the rate and we tried to get all the lenders—we tried to get everybody together in the room to come up with a compromise and they wouldn't do it and we finally had to settle on a rate. And the concern was if the rate—the margin was set at a rate sufficiently low, that the lending institutions would not have—many of them not have a desire stay in the business. The concern was that we would drive people from the business.

I'm really not concerned about the banks. I think banks will always do fine. I helped start one. I know how they function and they will always make a profit because there is some phase of the market they can go into and if student lending became less attractive, they would move out of it into another area and the feeling was that those who were able to control their costs, the large businesses probably that were able to control their costs the best would stay in the business.

And I remember that debate very specifically. The concern was if the smaller people got out of the business, those who went to community colleges and those who really needed the help the most, because a loan had to be about $7,000 before they made money and those who needed $500 or needed a thousand would be left out, that was a big concern in setting that rate.

And on the one side we'd get hit, well, you're helping the banks too much, you're making the rate too high and they're going to make too much money, and I kind of got painted like that and that was not my concern at all. The concern was keeping enough lenders in that everybody would have an opportunity of being served.

Time has changed. It's 5 years later and that probably isn't as big a concern but I think it's still a part of the concern because we have to always, I think, from our side try to make sure that there's going to be enough people in the business that enough students are being to be able to be helped.

The thing that's really driving me on this reauthorization is access. I think we have—that was the original intent of the law, to make sure that we helped those who needed the help the most and as many as possible. We've been beat up a little bit because we haven't increased the Pell grant limit but actually we put a lot more money into Pell grants. The limit has remained the same but a lot more people are benefiting from it.

And so when we're talking about having so much money—just so much money to use, we try to say how can we put it to where it's going to help the maximum number of people to have the most opportunity. And I'm sorry, Ms. Wasserman, but we're—I think in that debate we end up looking at who we can help get into the system rather than those who have already have and are benefiting from the system.

And anyway, this is going to be one of the things that drives us through this whole process. We'll have time to—we'll have some visits. You and I will have some talks.

Mr. Kildee.

Mr. KILDEE. Thank you, Mr. Chairman. I really think we have a great panel here. At one time they had difficulty electing a Pope so they put all the Cardinals in a room and gave them no food and they quickly decided who the Pope would be and I think that we could put you all in one room—I'd feed you, though—and have you agree—if you could agree on a bill—I do think we have a good cross section of people with a great deal of knowledge, a great deal of experience and I think have been very helpful to this Committee.

So I don't think we will lock you in that room but I do think we have the people who could probably reach an agreement on something that would be beneficial to both the lender and the borrower. You know, you can't have borrowers unless you have lenders. That's a very important factor and we arrived at that agreement fairly early at one of our breakfast meetings, I think, several years ago. We didn't know where to put the figure but we need both and I think—I really do appreciate the cross section we have here today.

Let me ask you one question, Mr. Morrow. Your testimony mentions that about 50 percent of graduating college students aren't even aware of their ability to consolidate. What can we do to address that?

Mr. MORROW. Well, I think there are a number of things we can do. We can strengthen the exit interview process which is a required step that students have to go through once they leave college. It's done now. I'm not sure that it's done to the best that it could be done.

For example, we actually send people, as does Sallie Mae and others, out to universities to walk graduating students through what options they have about repayment. I firmly believe, and again I've had three children put through college who have gone on to—I've paid the first four, they paid anything beyond that, and they took their loans.

And of course, having been in the business for 20 years, I'm always interested in what they're getting in the mail. Not one, not one lender ever talks about consolidation as a repayment option. They talk about flat repayment, they talk about graduated repayment, but when they get to repayment disclosure after that 6 months of grace, very seldom is it laid out as an option, if ever. I've never seen it.

Now, they might have changed—although I still have a daughter paying loans; I haven't seen it on her stuff. But that to me is—particularly if—back to the point about keeping customers. I mean, if you're doing a good job with your customer base—and I said this to a group of people a couple years ago and they weren't very happy with me, but the fact of the matter is it's a hundred times harder to get a new customer than to retain a customer.

If you're being fair to that customer and you've had them day one as a freshman, you're probably going to have them through 20 years or 10 years or whatever it is of their life. There's a lot of things about disclosure. In the written testimony I talk about we should beef up disclosure rules. There's a lot more information we could give to graduates about their full array of options on repayment.

Mr. KILDEE. Dallas, you mentioned the support of your organization for making Pell grants an entitlement. Why make it an entitlement? How would that—can you go into why that would give greater help to the students? I think I know the answer but I'd like to have you give it, for the record.

Mr. MARTIN. Well, Mr. Kildee, I guess we have felt for a long time that—for very needy students that loans can be helpful but grants make the difference with most of those students in terms of whether or not they're going to choose to go on with education. There's a lot of research that shows that for very low income families, many of them are very skeptical about taking out debt and so loans is really the access point for those families.

Our feeling is that the Pell grant program has been tremendously successful and what we would like to see is not only it be restored to its original purchasing power, which would be close to a doubling of what the maximum grant is now, but we would like to see it locked in as an entitlement so that it's predictable.

So when I could say to a young family or a student that's in middle school now that if you stay in school and you work hard and do this and press yourself by taking these kinds of challenging courses and so on, regardless of the fact that you have the financial means, when you graduate there will be an assurance that this grant will be there to cover this amount of your education and it would be indexed accordingly to give that predictability.

And I think that would be a great American promise to those kinds of young people that need that, that without that kind of assistance could not obtain a postsecondary education.

Mr. KILDEE. You know, the original GI Bill, that was a grant and we know that was successful. You've heard me say this, Dallas you've probably heard me say it hundreds of times, that on the east side of Flint no one went to college. That's where I was raised. No one went to college until the GI Bill of rights came around and it was a grant. It wasn't a loan, it was a grant and it enabled—it changed the future for those people.

Thank you very much.

Mr. MARTIN. You're welcome.

Chairman MCKEON. Thank you. Mr. Tierney.

Mr. TIERNEY. Thank you. I want to just ask Ms. McCormack to help me clear up one thing that I'm not certain on.

When Sallie Mae originates a loan, there's a cost obviously to that. Can you ballpark what that is on a particular loan?

Ms. MCCORMACK. There are multiple costs associated with those originating numbers. There's the actual cost—

Mr. TIERNEY. No, the total cost. What does it cost you to originate say a $10,000 loan?

Ms. MCCORMACK. I would have to get that information specifically to you but it's a combination of our investment and technology and infrastructure as well as the people processing of origination of the loan, the web technology as well as the funding costs associated with that.

Mr. TIERNEY. But you've got all that stuff in place already, right?

Ms. MCCORMACK. We do make significant investments.

Mr. TIERNEY. So we're talking about an additional loan comes in, the cost is a much lesser amount than trying to divide all of that—

Ms. MCCORMACK. On a prorated basis, that's correct.

Mr. TIERNEY. Now, during the period of time from when a student takes out a loan through the course of their college career, whatever, they do not make any payments on that, correct?

Ms. MCCORMACK. That's correct.

Mr. TIERNEY. Sallie Mae still makes a profit during that period of time; you still make some money, don't you?

Ms. MCCORMACK. We make interest spread on the loans during that period of time. That's correct.

Mr. TIERNEY. And if that's a 4-year loan, how much will that interest spread that you make exceed the amount that you invested in terms of originating that loan?

Ms. MCCORMACK. It depends on the size of the loan, the interest rate on the loan.

Mr. TIERNEY. Is it a healthy amount?

Ms. MCCORMACK. The bulk of the earnings for us are actually on the repayment side of the business—

Mr. TIERNEY. I understand that but, please, work with me here, will you? I mean, we can play tactic all day long but you know where I'm going and I'd like your help getting there just so we can have an honest discussion about this.

So what is the spread roughly on a loan of $10,000 between what you really spend on origination, not all your capital costs spread out forever, and what you get during that period of time on the spread?

Ms. MCCORMACK. I don't have that particular number at the top of my head but I will tell you that we—when we make investments

in the student loan program we assume the investment for the asset for the life of the loan and we assume a certain amount of prepayment risk on it.

Mr. TIERNEY. We're going to play tactic no matter what we do here, aren't you? I really would like you to work with me on this, try to get to a point instead of, you know, being argumentative but if we could go—

Ms. MCCORMACK. What is it you would like me to say?

Mr. TIERNEY. I'd like you to just give me an answer without giving me a lot of explanation and a tall tale. But the bottom line is there is money being made by somebody like Sallie Mae during that period of time. Am I correct?

Ms. MCCORMACK. Yes. Absolutely.

Mr. TIERNEY. So earlier when you told me that, gee, everybody is going to get out of the market and nobody will make these loans anymore, it makes it a little—a stretch for me to believe that somebody won't find it profitable to get into that market should you decide that all Sallie Mae wants to do is reconsolidate or consolidate.

Ms. MCCORMACK. Mr. Tierney, I would venture to say that someone would try to enter that piece of the business. However, Sallie Mae would be incented to work in the back end of the business in reconsolidation—

Mr. TIERNEY. You said that, but you also implied that nobody else would get in there and I don't think that's correct. I think that somebody else would go in there because there is some degree of money to be made on that and I wanted to clarify that because I think that's the case.

I mean, you may decide that you want to get out and go somewhere else but there is money being made and we can anticipate that somebody—

Ms. MCCORMACK. What will happen is the investment in helping students understand how to pay for college, educating them on the forms of financing available for college, the kinds of things that really cost a lot of money for a company like Sallie Mae will not be made as investments if the major benefit is on the back end of the program in terms of reconsolidation.

There definitely will be less money spent to help borrowers get into school and to stay in school.

Mr. TIERNEY. We can assume others might step forward and do that, too, right?

Ms. MCCORMACK. I don't know.

Mr. TIERNEY. Mr. Morrow, does that create a problem for you, Sallie Mae going into the reconsolidation market and students being left without any advice?

Mr. MORROW. Would that be a problem for me?

Mr. TIERNEY. Well, for students. What do you say to that?

Mr. MORROW. I tend to agree that if competition is allowed, that people will find a way to make it happen. People said a few years ago that we were going to destabilize the business by direct to consumer market of the consolidation options. I don't think we've seen any destabilization of the market.

There are many people in the business today who do just the in-school lending as you're saying and sell as it moves into repayment at the back end. That's a fairly common practice in this business,

has been for the 20 years that I've been in this business, so I think people are making something. If they don't want to stay in the repayment business, they're selling out on the secondary market and still making fairly healthy margins. I don't see—

Mr. TIERNEY. Mr. Wozniak, is that because—you can confirm that, Mr. Wozniak?

Mr. WOZNIAK. I think what Mr. Morrow is talking about is the lenders in the marketplace originating loans and selling to the secondary market. In part that's what just about any of the top holders do—do acquire loans in the secondary market.

Mr. TIERNEY. Thank you. Dr. Martin, do you want to add anything?

Mr. MARTIN. You know, Mr. Tierney, I think the question is—and I think you're right. There's no—I don't know what the spread is and I suspect if you look at different lenders you're going to find that, depending on their volume and their level of sophistication, that their margins are going to be different but yes, they are making some profit.

The question is, however, if we change this around too much, it's not that some may not step in. The question is will we have enough capacity to take care of all the students that we need. I mean, we have spent a lot of years trying to very carefully work through the student loan industry to build it up so that we have a system now that—you know, I think it's a great system from the standpoint that there's no problem with people being able to go out and get loans.

And I remember the days when we were struggling and had shortfalls of when not everybody could or certain students in certain sectors could not get loans. So I think there is a fine balance and I would hate to see us turn it all over on the back end, even though I think there's some benefits.

I think there are some other things that we ought to look at along with consolidation. I do think that graduates have trouble many times when they're first coming out of school about being able to meet their loan payments. And it's not that they can't maybe the third or fourth year out. It's that first two or 3 years that they're getting settled that they have the most difficulty.

I think there are some other things that we can look at through repayment terms and so on as a part of the programs that might help soften that a little bit so it would make it easier on graduates that had those high debts.

I also think—and we've recommended this to you and Mr. Miller, I think, has proposed this same thing. One of the things that we looked at, we talked about the interest deduction. The problem is interest deduction doesn't work real well for a lot of borrowers when they first come out of school because they're not making enough to itemize their income tax to be able to deduct the interest.

What we would propose is turning that into a credit so that the interest that they pay would become a refundable credit that actually could go to help pay part of their loan. Now, that's—in my opinion, something like that might be more feasible in terms of spending the money than some of this money that we'd be spending

with the other part of it on the subsidies that we're paying in consolidation.

But I would like to have more discussion and look at all of the alternatives and I hope that that's what is going to occur during this reauthorization so that we come out with the best public policy that there is.

The other thing I was going to remind Mr. Morrow of was—I thought it was interesting because I agreed with him about the young lady that he was talking about that wanted to come back and work for him but had all this student loan debt. Well, if she was going to work with them over at the Department of Education, they have the ability there to give loan cancellations to people that come to the government agencies. If she had wanted to come to work for me, I wouldn't have had that provision because I don't have such an authority under my agency that's a non-profit. But maybe that was the variable—

Mr. MORROW. No. She wanted to stay in Boston.

Mr. TIERNEY. She also had—

Chairman MCKEON. Time has expired.

Mr. TIERNEY [continuing]. Had to pay on the value of that on taxes so we have to deal with that problem, too. Thank you all.

Chairman MCKEON. Mr. Burns.

Mr. BURNS. Thank you, Mr. Chairman. I have no further questions and appreciate the input from the panel.

Chairman MCKEON. That will then terminate our panel this morning. We thank you for being here for your testimony and ask you to stay involved as we go through this process because we'll have a lot of discussion as we go forward and we will get that question to you in writing and I'd appreciate if you could respond.

Thank you very much. This Committee stands adjourned.

[Whereupon, at 1:24 p.m., the Subcommittee was adjourned.]

[Additional material submitted for the record follows:]

Statement of Hon. Joe Wilson, a Representative in Congress from the State of South Carolina

Mr. Chairman, I want to thank Mr. Regula and Ms. DeLauro for taking the time to testify on these important issues. Earlier this year we successfully passed two pieces of legislation that will help teachers to pay for their education. Loan forgiveness is a key step to attracting highly qualified teachers. For those who will continue to need student loans, we need to make sure those loans are as affordable as possible. Student loans have never in the history of the program been more affordable than they are today. Low fixed rate consolidation loans are a key component to that effect. For most student loan borrowers, they need to make their monthly rent and other payments. Consolidation loans make their student loan burden affordable. As I said two weeks ago, one of the major hindrances to affordability is the Single Holder Rule. It simply gets in the way of recent college graduates from accessing the full array of competitive student loan programs. For that reason, I am asking this Subcommittee to repeal the Single Holder Rule. Additionally, I am concerned about borrowers who locked in interest rates two or three years ago and cannot reconsolidate that debt. This Subcommittee should attempt to remedy the problem of reconsolidation as quickly as possible. We must help consumers where we can. Mr. Chairman, thank you for your leadership.

Response of June McCormack to Questions Submitted for the Record

QUESTIONS FROM HON. PETE HOEKSTRA

I have heard from Sallie Mae and others that consolidation will have significant taxpayer cost in the out years. As a former member of the House Budget committee and a fiscal conservative, this is something that concerns me.

I was impressed by the Ernst & Young work that indicates that Consolidation Loans will be a net Federal payor while it is clear that Stafford loans, and in particular Stafford Loans with extended repayment, will require huge taxpayer subsidies.

With that said, isn't it true that the Higher Education Act proposal signed on to by Sallie Mae calls for expanding extended repayment?

And, as we know, increasing the availability of Extended Repayment lessens the need for Consolidation Loans and reduces the taxes paid in by lenders.

Why should this Committee increase extended repayment and spend more than $1 billion in lost revenue?

Response: While we have not reviewed the Ernst & Young work, we have reviewed the claim that on a cash basis the consolidation program has returned $1.4 billion to the Treasury over the past seven years. However, $1.4 billion only represents the fees generated by the consolidation program. It does not count the costs to the government of interest subsidies, default claims, and collection costs. The net cost of the consolidation program has been $1.5 billion over the past seven years. Further, while consolidation loans have been 26% of the loan volume over the past seven years, consolidation fees have only represented 21% of the total fees collected.

Quoting the cash cost of the consolidation program is extremely misleading because it does not reflect the cost the government will incur from today's low-rate consolidation loans. The cost of these loans will show up as the federal government subsidizes payments over the next 20 to 30 years. For just the consolidation loans made at last year's interest rates, the cost will be between $3 and $5 billion, depending on how many loans actually consolidate.

While we have not reviewed the Ernst & Young work, we would note that whether or not extended repayment saves or costs really depends on the interest rate environment. In the current interest rate environment, the federal cost would be greatly reduced if borrowers had greater choices to extend repayment with the Stafford loans rather than consolidating and shifting their interest costs to the federal taxpayer. Further, Sallie Mae does support expanding extended repayment terms to borrowers for good policy reasons. The standard ten-year repayment period has been in place since student loan program was created in 1965. As loan balances have increased, we are finding the ten-year term to be insufficient for some borrowers and believe that more repayment flexibility is needed. During the last reauthorization, extended repayment was made available only for new borrowers with loan balances above $30,000. We support expanding this to align it with the tiered repayment-terms contained in the Higher Education Act (HEA) current law for consolidation loans.

We believe that borrowers should be encouraged to repay their loans as quickly as possible. Unfortunately, today the only option many borrowers have for extending their repayment term is through the loan consolidation program, which often extended borrower repayment longer than is necessary, increasing total cost of the loan to a borrower. Introducing more repayment flexibility into the loan program will help keep extra borrower interest rate expense to a minimum and would add much needed flexibility to the program.

Additionally, why did Sallie Mae leave the consolidation program during the second half of 1997 and the first half of 1998?

Response: For a brief period—November 1997 through September 1998—Sallie Mae suspended its participation in the loan consolidation program. This suspension was due to a temporary legislative change made in consolidation program, which changed the interest rate formula but failed to adjust the fee structure, making the program uneconomical from our perspective. Congress recognized the flaw in the consolidation structure at the time and moved to resolve the matter as part of the 1998 HEA reauthorization. Once this legislation was enacted, we immediately reentered the loan consolidation market place.

During this period, we insured that our borrowers continued to receive repayment relief. Borrowers who needed consolidation loans were referred to other FFELP lenders or the Direct Loan program. We also developed a new repayment product to assist borrowers who needed payment relief, called a FLEX Repay account. Under the terms of this program, we were able to extend the borrower's repayment term from three to five years, enabling borrowers to lower their payments. Importantly,

this also insured that borrowers avoided locking in the high rates, which were in effect at that time, and permitted them to take advantage of our borrower benefits.

QUESTIONS FROM HON. JOE WILSON

I want to congratulate Ms. McCormack and Sallie Mae. Yesterday, Sallie Mae reported that for the six months ending June 30, the company's earnings were $789 million. I also saw that consumer reporter Michael Singletary recently ran an article on reconsolidation. I know that the Special Counsel to the Consumer Bankers" Association was quoted as saying lenders "have high yielding assets that they do not want to lose." I have a question for Mr. Morrow and Ms. McCormack. Shouldn't Congress support wide ranging competition including repeal of the single holder rule and allowing borrowers access to these low rates?

Response: We support vigorous competition in the student loan program to make sure that students and their families have access to the best services and products possible. Repeal of the single holder rule has nothing to do with providing students either of these. Because consolidation rates are determined by statute, all lenders offer the same rate. Repeal of the single holder rule has nothing to do with the eligibility to consolidate one's student loans. Anyone who wants to consolidate his or her student loans today can do so.

Consolidation marketers who are promoting the repeal of the single holder rule do very little to invest or compete in the program where it is needed most—when students entering college need access to financial aid. The financial aid community and Congress depend on us and other student loan lenders to provide capital, to pay up front fees, and invest in a technology network that processes loans and data in seconds. Most of this investment takes place four years before the average student makes the first payment. Loan providers make this investment because there is some level of certainty that we will have the return on the asset of earning interest after the student graduates. Without such assurance, lenders would be rewarded to be in the consolidation business, not the student loan business.

The single holder rule assures that lenders provide those critical services to students and schools. Further, the rule was designed to protect borrowers from predatory telemarketing efforts. That has turned out to be a prophetic fear. We, along with our school clients, hear from borrowers who have been told misleading, confusing or inaccurate information from certain consolidation marketers. Repeal of the single holder rule will do nothing for the student loan program, or existing students other than unleash an avalanche of spam, junk mail and telemarketers, some pushing misleading information. Attached for the record is a recent posting from FINAID.

I know that some of the stakeholders in the student aid programs have encouraged Congress to go back to "first principles" in the Consolidation Loan Program. The early version of the consolidation program was less competitive and less attractive to borrowers. It was created more than 20 years ago at a time of low student loan debt. However, borrowers have much higher debt and a large desire for consolidation loans, so much so that they are seeking to consolidate and in some cases refinance. If we went back to first principles in the student loan program it would be a paper driven program with as much as a month before loans were to fund. This is really a question for all of the witnesses. Rather than go back to a forgone era, shouldn't we try and make all the programs better and more borrower friendly?

Response: We do not believe that bringing the loan consolidation program back to its intended purpose would in any way turn back the advancements made in the student loan program. Today's student loan program serves more students, more efficiently at the lowest cost to the taxpayer in the history of the federal student loan program. Sallie Mae, like most of today's loan providers, has invested in Internet-based services that provide fast, reliable services for borrowers. Thanks to these investments, students can now receive their loans on the same day they apply—all at the click of a mouse. Only a few years ago, this same process took weeks. Loan providers are also adding web-based tools and services every year that allow students to quickly and easily estimate their college costs, compare repayment options, check their loan status, learn about managing debt and obtain information on debt counseling.

Response of Barry Morrow to Questions Submitted for the Record

QUESTIONS FROM HON. JOE WILSON

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I couldn't agree with you more, Congressman Wilson. As I noted in my prepared testimony, the situation college students and graduates face today is strikingly different from that in 1986, when the current consolidation program was authorized. Back then, when computers were in their infancy, the average debt level was a small fraction of today's $19,000 for a graduate with a bachelor's degree. Back then, federal grants paid a greater portion of college costs than loans for needy students. Today, loans are a necessity for Pell recipients along with all others.

Some have testified that, once students graduate, our obligation to help them pay for college is over. The reality is that we have created a system for paying for higher education that shifts the day of reckoning to the years following graduation. We have convinced millions of students that a college degree is essential, and that it is worth going into debt over. To say to them after they graduate "Too bad—you're on your own" would be to perpetrate a cruel hoax on America's youth. The word would soon get out that a college degree is NOT worth the financial distress that follows. Consolidation is the mechanism Congress fortuitously created that allows graduates to cope.

Perhaps in 1986, the era of "first principles," consolidation could be viewed as a convenience for a small category of graduates. In 2003, it is, for many, an essential tool for making ends meet. The program should be as widely available and borrower-friendly as Congress can make it.

I want to congratulate Ms. McCormack and Sallie Mae. Yesterday. Sallie Mae reported that for the six months ending June 30, the company's earnings were $789 million. I also saw that consumer reporter Michael Singletary recently ran an article on reconsolidation. I know that the Special Counsel to the Consumer Bankers' Association was quoted as saying lenders "have high yielding assets that they do not want to lose." I have a question for Mr. Morrow and Ms. McCormack. Shouldn't Congress support wide ranging competition including repeal of the single holder rule and allow borrowers access to these low rates?

I totally agree with you, Congressman Wilson. Congress should indeed support wide-ranging competition in loan consolidation—the same level of competition that exists for the Stafford and PLUS loan programs, where students and their parents are guaranteed, by law, the right to deal with the lender of their choice. We have been promoting repeal of the single holder rule as long as our company has been in existence. We believe that college graduates should be able to deal with the consolidation lenders of their choice. If one lender offers better borrower benefits (e.g., a lower interest rate) to a student loan borrower wanting to consolidate, then that consumer should be able to consolidate with that lender—no matter how few or how many lenders he has loans with. If another company is offering a better product, the customer should be free to consolidate with them.

There are many factors that may influence graduates" desire to deal with someone other than their current lenders. For instance, as you may know, the nation's largest holder of student loans recently admitted it has erroneously calculated the payment plans of over 800,000 of its customers. Many of those borrowers are being required to pay drastically increased monthly payments as a result in order to pay their loans off in the time permitted by law. Consolidation is a way many of those consumers could find someone to better manage their student loans—but not for those having all of their loans at that company.

With regard for reconsolidation, as I mentioned in my prepared testimony, we are prepared to substitute a lower-yielding asset for a higher-yielding asset if that is what is best for students. The student loan programs are there to allow students to get college educations in the most cost-effective manner possible, not to provide lifetime profit guarantees to the lenders that make and hold the loans.

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