Loyola Consumer Law Review

Volume 22 | Issue 4 Article 7

2010

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HEALTH CARE REFORM IMPACTS STUDENT LENDING AND PELL GRANT PROGRAMS

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I. Introduction

A lot of publicity has surrounded the impact of H.R. 4872, The Health Care Reform Act ("Act"). Logically, the publicity has focused on what the Act will do to the current health care system. With the impact this Act has on health care reform, it is not surprising that very little publicity has been given to the changes the Act will have on the federal student lending program.

President Obama discussed how the bill will impact student lending in one of his weekly radio and internet broadcasts.[1] Obama hopes this legislation will be a step in the right direction of meeting his goal that by the end of the decade, the U.S. will once again have the highest proportion of college graduates in the world.[2]

Earlier in the Obama administration a law aimed at the federal student loan program called the Student Aid and Fiscal Responsibility Act stalled in the Senate.[3] However, legislators were able to include many of the student loan changes they desired in the Health Care Reform Act. Title II of the Health Care Reform Act is entitled "Education and Health." Subtitle A of Title II is devoted to Education. Part I of Subtitle A is entitled "Investing in Students and Families" while Part II is entitled "Student Loan Reform."[4] If you are wondering what "Investing in Students and Families" and "Student Loan Reform" has to do

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[1] Steven Thomma, *President Obama: New Law Will Help Students Pay for College*, BOSTON HERALD, March 28, 2010, *available at* http://www.bostonherald.com/news/us_politics/view.bg?articleid=1242829.

[2] *Id.*

[3] Carmen Lu, *Direct Loans Bill Stalls*, YALE DAILY NEWS, February 9, 2010, *available at* http://www.yaledailynews.com/news/university-news/2010/02/09/direct-loans-bill-stalls/.

[4] H.R. 4872 – 111th Congress: Health Care and Education Reconciliation Act of 2010 (2010).

with health care reform, you are not alone. [5]

The supporters of the Act claim this to be the most significant change to student lending in a generation.[6] The bill will affect students in three major ways. First, the bill will change how students borrow funds from the government. Second, the bill will reinvigorate the Pell Grants program, and third, the bill will cap student loan repayments of federal loans at 10% of the borrower's income.[7]

II. What the Health Care Reform Act Does for Students

For decades, the Federal Family Education Loan ("FFEL") program has been responsible for giving subsidies to banks and lenders who then disperse the funds to student borrowers.[8] Under this new bill the FFEL will be eliminated.[9]

A. Elimination of the Federal Family Education Loan Program

The federal student loan program was created in 1965, and until now, the student loan program included the FFEL and the Direct Loan program.[10] While the FFEL supplied subsidies to lenders, the Direct Loan program has been dispersing loans directly to student borrowers since 1993.[11] Even though lending institutions were initiating the loans to student borrowers under the FFEL program, the government still bore the majority of the risk of default by guaranteeing up to 97% of any defaulted loan.[12]

The Act eliminates the annual $60 billion FFEL program where the government supplies subsidies to lenders and lenders in turn lend funds to students.[13] Essentially, a middleman is eliminated. According to the Congressional Budget Office the

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[5] Charles A. Jaffe, *Health Care Bill Lessens Burden on Student Loans*, NJ.com, March 29, 2010, *available at* http://www.nj.com/business/index.ssf/2010/03/health_bill_lessens_burden_of.html.

[6] Daniel de Vise, *House Approves Huge Changes to Student Loan Program*, THE WASHINGTON POST, March 22, 2010 at A01.

[7] Thomma, *supra* note 1.

[8] Gilbert Cruz, *Student Loans Get a Government Takeover*, TIME, April 5, 2010.

[9] H.R. 4872, *supra* note 4, *see* § 2205.

[10] Cruz, *supra* note 8.

[11] *Id.*

[12] *Id.*

[13] de Vise, *supra* note 6.

elimination of lenders acting as middlemen will save $61 billion over 10 years.[14] Thirty-six billion dollars of the estimated $61 billion in savings will be used for the Pell Grant program.[15] Smaller portions of the $61 billion in expected savings would be used to reduce the deficit and supply funding for other initiatives such as promoting community and historical black colleges and placing a cap on loan payments.[16]

The elimination of the FFEL was not a surprise to everyone. The Direct Loans program started lending directly to students in the early 1990s in part because of allegations of corruption.[17] More recently, the private lending industry has been accused of overcharging the government and offering colleges incentives to steer students to their loans.[18]

Previously, it was not the student but the college or university who decided which lender would originate federal loans for their students.[19] With the elimination of FFEL, this choice is being eliminated. However, the loans will now come directly from the Department of Education and will have the same terms and conditions as those loans previously supplied through private lenders.[20]

Because the elimination of the FFEL program means more money for the Pell program, the higher-education industry has supported the transition.[21] Additionally, many college and universities have already switched to the Direct Loans program in anticipation of the change to the FFEL program.[22]

However, not all schools have made the transition to the Direct Loans program. The bill includes $50 million in funding to schools to assist in the transition to the Direct Loans program.[23] One thing that this $50 million may be used for is the signing of a new master promissory note. Students at schools that did not previously participate in the Direct Loans program will need to

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14 *Id.*
15 Cruz, *supra* note 8.
16 de Vise, *supra* note 6.
17 *Id.*
18 *Id.*
19 Jaffe, *supra* note 5.
20 *Id.*
21 *Id.*
22 Monica Martinez, *Student-loan Reform Slid Into Health Law*, THE WASHINGTON TIMES, March 29, 2010, available at: http://www.washingtontimes.com/news/2010/mar/29/student-loan-takeover-slips-through-with-health-ca/.
23 *Id.*

sign a new promissory note and complete a new entrance counseling session and exam.[24]

Parents will also benefit from the removal of a middleman from the student lending program. Under the new program, Parent PLUS loans will be capped at 7.9 percent compared to the current cap of 8.5 percent with private lenders.[25]

An additional incentive to borrowers is the fact that the process will call for one payment to be sent to one lender, the government.[26] However, even thought the government is originating the loan, and payments are being made to the government, the loans will actually be serviced by private lenders.[27] Private lenders will bid on the contract to service the loans and they will be required to use domestic employees to service the loans.[28]

Furthermore, under the new program, student loans will not be securitized, meaning that the loans cannot be sold to other banks.[29] No longer will students receive letters in the mail notifying them that their loan has been sold and payments must be made to a new lender.

B. Change to Repayment Process

Another important change to the student loan program is a change in the repayment process. Under the Act, any new loan made to a new borrower on or after July 1, 2014 will be able to apply for a program that caps monthly loan repayments at 10% of the borrower's monthly income ("income based-repayment"), and decreases the payment period from 25 years to 20 years.[30]

Additionally, existing loans that are participating in the income based-repayment program will have the monthly payments capped at 15 percent of the borrower's income.[31] Furthermore, if there is a loan balance remaining after 20 years of payments any remaining balance may be forgiven.[32]

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[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] Jaffe, *supra* note 5.
[28] *Id.*
[29] *Id.*
[30] H.R. 4872, *supra* note 4, *see* § 2213.
[31] Martinez, *supra* note 22.
[32] Jaffe, *supra* note 5.

C. Pell Grants Program Saved

Pell grants originally covered two thirds of tuition at a public university when the program was started in 1973.[33] Today, Pell grants only cover about one-third of the tuition cost at public universities.[34] It was expected that the Pell program would run out of money this year resulting in the cutting or the elimination of Pell grants to as many as 8 million students.[35]

Of the estimated $61 billion in savings from the elimination of the FFEL over the next decade, $36 billion is to be used for the Pell grant program. [36] The bill specifically provides for $13.5 billion in funding for Pell grants in 2011.[37]

Currently, the maximum Pell grant is $5,550 a year.[38] However, now the Pell grant program will be linked to the Consumer Price Index and could reach a maximum amount of $5,975 by 2017.[39]

III. Conclusion

Over the years it has become clear that reform was needed in the student lending and Pell grant programs. Reform was unsuccessful in the Student Aid and Fiscal Responsibility Act and came instead in the Health Care Reform Act. Time will tell if eliminating private lenders as middlemen will provide the expected savings. However, it is clear that the Health Care Reform Act will revitalize and ensure the continuance of the Pell grants program utilized by low to middle class students.

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[33] de Vise, *supra* note 6.
[34] *Id.*
[35] Jaffe, *supra* note 5.
[36] de Vise, *supra* note 6.
[37] H.R. 4872 *supra* note 4, *see* § 2101.
[38] Jaffe, *supra* note 5.
[39] de Vise *supra* note 6.