



# nassgap

## Washington Update – Spring 2013

As spring comes to Washington, so does a welcome new trend, bi-partisan bills. Whether they pass or fail, it is good to see folks coming across the aisle to try and make things work. While the Manchin-Toomey effort on background checks didn't make it to the finish line, it will be interesting to watch progress on the pending immigration initiatives. And then, next up, is most likely the student loan rate fix v2.0.

We'll get to that issue later, but first, a recap of how activities in Washington have shaped higher education funding so far this year.

### Federal Fiscal Year 2013 Budget

Currently, the federal government is operating on a "continuing resolution" that passed in March, through the end of the federal fiscal year, September 30, 2013. Generally, education and other programs are funded at the prior year's levels but subject to sequestration.

### Sequestration

Mandated across the board reductions in federal spending took effect at the beginning of March and most education programs are affected, although due to the "forward-funded" nature of many education programs, the impact will not be felt until the 2013-14 academic year begins. While Pell grants are exempt from sequestration for FFY 2013, Supplemental Education Opportunity Grants and College Work-Study are impacted; funding cuts to these programs will likely fall in the 5.2-5.5% range if not repealed, but the impact will vary by institution, as the programs are formula-funded by institution. The impact on students will vary as well, since colleges have discretion in terms of how to apply the cuts – they can cut all awards pro rata across all students, or they can eliminate awards for students with the smallest need, among other options.

I mention "if repealed" because uproars over the impact of certain cuts caused Congress to act in a rapid, bi-partisan manner to repeal cuts affecting meat inspectors, air traffic controllers, and a couple other programs. The most significant repeal to date, at least for higher education, was actually in the Defense Department's budget. They had eliminated funding for any new grants – for new and existing students – in the military's Tuition Assistance Program, which enabled active duty military members to take college courses. Congress mandated that funding for this program be fully restored. Because most of the cuts for higher education in ED's budget don't kick in until this summer, it will be interesting to see if Congress responds to the tens of thousands of students whose SEOG

and CWS grants will be cut or eliminated for the fall 2013 semester and beyond. Keep in mind that sequestration is a multi-year event, not a one-time reduction.

#### Fixed, Variable, or Variable Fixed?

The interest rate on Subsidized Stafford loans is once again set to double from 3.4% to 6.8% on July 1, 2013. There are multiple bills and proposals in play to address this issue. Senator Reed (D-RI) and Representatives Courtney (D-CT) and Bass (D-CA) have offered bills to keep the rate at 3.4% either temporarily – for another year or two to allow Congress to fully evaluate long-term solutions for the rates – or permanently. Others including the President, in his FFY14 Budget, and Senators Coburn (R-OK), Burr (R-NC), and Alexander (R-TN), in legislation, propose to set interest rates annually to a “market rate” based on the 10 year Treasury note (10 Yr T), which in late April has been ranging from 1.6-1.8%.

While the market rate, once set, would be fixed for the life of that loan, each subsequent loan’s interest rate would be determined based on the most recent 10 year Treasury rate (in the past, the last Treasury auction in May has set the rate for the upcoming academic year). Some folks refer to this concept as a “variable fixed rate”. Historically, Stafford interest rates have been fixed, except for a period in the 1990’s through June 30, 2006 when interest rates were variable, based on 91 day Treasury bills plus a margin or “spread” that ranged from 1.7% to over 3%, but with an interest rate cap in place that most recently prevented loan interest rates from rising higher than 8.25%. Some are advocating a return to these variable rate loans, but as of late April, this option seems the least likely outcome for resolving the Stafford rate issue by July 1st.

Given that the President and Republicans in the Senate have proposed the “fixed variable” market rate option, one might think that represents a consensus, although their proposals vary with regard to the spread above the 10 Yr T. The President’s proposal recommends a spread of 0.93% for Subsidized Stafford, 2.93% for Unsubsidized Stafford, and 3.93% for PLUS (Parent and Grad), resulting in rates of about 2.6%, 4.6%, and 5.6%, respectively, as of late April. The Coburn-Burr-Alexander proposal includes a spread of 3% for all loans, resulting in about a 4.7% rate as of late April. Because the proposals result in rates higher than those today in the “out” years (e.g., 2018-2022), these proposals are directionally budget-neutral. Any effort to extend the 3.4% rate would be costly and require a budget “pay for”.

Those higher out year rates and the absence of a rate cap are the reasons that the variable fixed approach has not reached consensus status. As noted before, variable Stafford loan interest rates historically have been capped at 8.25%, and neither of the variable fixed proposals includes a rate cap. US-PIRG’s student advocate, Ethan Senack, described the proposals without rate caps as robbing Peter’s little brother to pay Peter. Many Democrats in the Senate and House agree with him.

Other than a federal budget, addressing the Stafford interest rate may be the only “must pass” legislation for higher education in 2013, with the reauthorization of the Higher Education Act likely deferred until (at least) 2014. One other legislative update of note is

the Smarter Borrowing Act, introduced by Senator Harkin, Chairman of the Senate HELP Committee, along with nine co-sponsors. This Act would require schools to verify that students and parents fully understand the loan terms and conditions and their payment options. Even in a challenging economy, it's hard to understand why default rates are rising when the Income-Based Repayment option is available to all Stafford borrowers.

#### Federal Fiscal Year 2014 Budget

The President's FFY14 budget proposal includes most of the new initiatives in the President's 2013 budget, such as an expansion of the Perkins loan program, Race To The Top for higher education, and the "First-in the-World" initiative. None of these initiatives were acted upon, much less passed, in either chamber of Congress in the past year.

#### Saving the Best News for Last!

The Pell Grant program is fully funded for the 2013-14 academic year, and is now projecting a surplus, not a shortfall for the 2014-15 year (which is funded in the FFY 2014 budget). While a small shortfall is currently projected for the 2015-16 academic year, the forecast has improved significantly in the past year.