



Testimony by Chancellor David G. Carter
Connecticut State University System (CSUS)
Before the Banks Committee &
Higher Education and Employment Advancement Committee
Wednesday, September 10, 2008

Good afternoon, Senator Duff, Representative Barry, Senator Hartley, Representative Willis and members of the Banks and Higher Education and Employment Advancement Committees. Thank you for inviting me here today to provide testimony on behalf of the Connecticut State University System (CSUS). I commend the committees for calling this informational forum, and for focusing the state's attention on the effect of the subprime mortgage crisis on the availability of funds for student loans.

With me today is James Schmutter, President of Western Connecticut State University (WCSU). I will make some general comments about the effect as evidenced by the experiences of the Eastern, Central, Southern and Western Connecticut State Universities and then President Schmutter will provide more specifics about the experience at Western. Finally, I have attached some background on federal and private loans for your information.

Let me begin by providing some context. The current subprime mortgage crisis is exacerbating an already unstable, unwieldy, inequitable and ineffective financial aid system in this country. We run the risk of this crisis becoming the straw that breaks the camel's back, if we are not diligent in understanding the potential impact, and working together – in Connecticut and nationally.

U.S. News recently observed that “the American dream is founded on the notion that anyone who is smart and disciplined can get an education and succeed. But the financial aid system meant to help needy students afford college is cracking under the strains of skyrocketing tuition and a crumbling economy.” The result is that “some smart, diligent, but relatively poor kids are being priced out of college.” And I would add that as the lending crisis continues, we can add middle class to that result as well.

Just this week, NBC News reported that the number of students applying for federal aid in the first half of this year jumped 16.3 percent as compared with the same period a year ago. The president of the National Association of State Student Grant and Aid Programs, Marilyn Cargill, recently said that “the only way many families paid tuition bills in recent years was with loans. But the credit crunch has wiped out many families ability to get a second mortgage or private education loan.” She described the current situation as “scary,” and I agree.

It is truly frightening for students and families working diligently to piece together the thousands of dollars necessary to pay for the higher education they'll need to succeed in today's world. And the pressures on students are often unbearable – especially the substantial percentage of our students who balance work and study, who are the first in their family to attend college, or who are raising a family and paying a mortgage in

addition to funding their education. We risk losing them, and as a society, we can't afford to.

A report by the non-partisan Congressional Research Service earlier this year highlighted the flaws in the current system, and an analysis by Student Lending Analytics concluded that students appear to be paying a penalty for the turmoil in the student-loan marketplace, as they find a reduced ability to obtain private loans that they have come to depend on.

That is an important aspect of what's happening. The statistics you hear in today's testimony regarding student loans can only begin to tell the full story. Beyond the direct impact on the student loan market is the impact on a family's ability to obtain home equity loans, which increasingly have become an important source of tuition funding. And since families are under no obligation to tell us about those loans, we cannot easily quantify that aspect of the problem – but we know it's out there. As a result, the true impact of the subprime mortgage crisis may not be known.

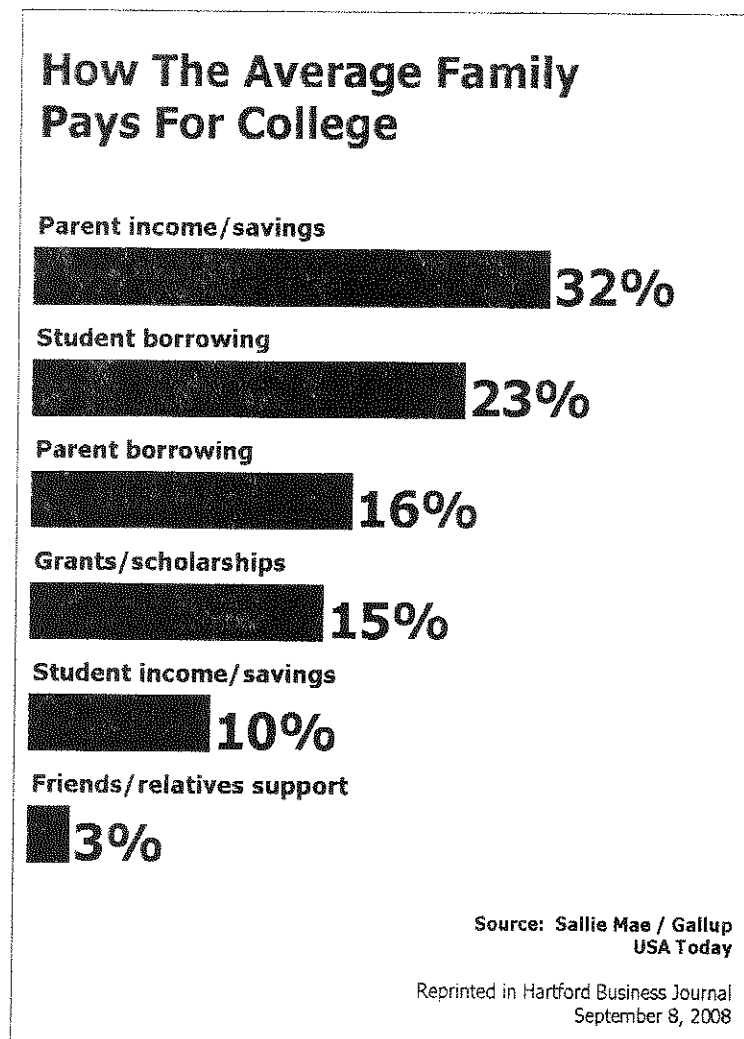
Let me make a number of other points before turning to President Schmotter:

- There appears to be a fair amount of confusion among students, understandably, as some banks that participated in the past drop out of the student loan program, or change borrower benefits, making them less favorable to the borrower. At times, it has seemed like “here today, gone tomorrow” has been the best way to describe what's been happening. And when it comes to education, that's not the approach our students deserve.
- Generally, the financial aid directors at the universities are as busy as they've ever been, helping students and families navigate this crisis. And they have received larger aid requests from some students, often because parents simply cannot get alternative loans.
- A survey of financial aid officers in this region, undertaken by the New England Board of Higher Education, found that although loans remain available, “there has been a distinct shift and increased in applications for parental PLUS loans, compensating for the contraction in the availability of private or alternative loans.”
- It appears that alternative lenders may be tightening their qualifications, and may be hiking rates for less qualified borrowers. For example, origination fees – while the maximum that could be charged has been 2.5 percent in the past, lenders would routinely waiver or lower them. Now banks are charging the full 2.5%. These are paid up front, and the net effect is to decrease the amount of funds going to the student. However, the student still has to repay the full gross amount borrowed. As a result, more students are not paying their bills on time – because they don't have the money to do so.

- As the crisis deepens, fewer banks - especially smaller ones - are offering alternative loans. As equity diminishes and standards get tougher, much-needed loans become unattainable for more and more families.
- And, as we know, federal loans have not increased nearly enough to cover the widening gap between supply and demand in alternative loans.
- I've also attached a chart with my testimony, which appeared in USA Today and the Hartford Business Journal, which clearly outlines how the average family pays for college.

Let me stop there, and turn it over to President Schmutter to continue. As many of you may recall, before coming to Western, President Schmutter served as dean of the College of Business and Economics at Lehigh University as dean of the Haworth College of Business at Western Michigan University. So, he knows of what he speaks.

Thank you very much.



Student Loans: Background

Federal Student Loans

Stafford Loans are for undergraduate, graduate and professional degree students. You **must** be enrolled as at least a half-time student to be eligible for a Stafford Loan. There are two types of Stafford Loans: subsidized and unsubsidized. You must have financial need to receive a subsidized Stafford Loan. Financial need is not a requirement to obtain an unsubsidized Stafford Loan. The U.S. Department of Education will pay (subsidize) the interest that accrues on subsidized Stafford Loans during certain periods. These loans are made through one of two U.S. Department of Education programs:

1. William D. Ford Federal Direct Loan (Direct Loan) Program

Loans made through this program are referred to as **Direct Loans**. Eligible students and parents borrow directly from the U.S. Department of Education at participating schools (CCSU is a direct lender, the other CSUS schools are not). Direct Loans include subsidized and unsubsidized Direct Stafford Loans (also known as Direct Subsidized Loans and Direct Unsubsidized Loans), Direct PLUS Loans, and Direct Consolidation Loans. These loans are repaid directly to the Federal Government.

2. Federal Family Education Loan (FFEL) Program

Loans made through this program are referred to as **FFEL Loans**. Private lenders provide funds that are guaranteed by the federal government. FFEL Loans include subsidized and unsubsidized FFEL Stafford Loans, FFEL PLUS Loans and FFEL Consolidation Loans. These loans are repaid to the bank or private lender that made the loan.

Stafford Loans (Direct and FFEL)

The Maximum Annual Loan Limits depend on:

- What year you are in school.
- Whether you are a dependent or independent student.

Subsidized Stafford Loan

- Available to students who demonstrate financial need.
- Eligible students can borrow a subsidized Stafford Loan to cover some or all of their need.

For a *subsidized* loan, the U.S. Department of Education pays the interest:

- ☐ While you're in school at least half-time.
- ☐ For the first six months after you leave school (referred to as a "grace period").
- ☐ During a period of deferment (a postponement of loan payments).

The amount of your subsidized loan cannot exceed your financial need.

Unsubsidized Stafford Loan

- Does not require students to demonstrate financial need.
- The U.S. Department of Education does not pay interest on unsubsidized loans.

For an *unsubsidized* loan:

- You're responsible for paying the interest that accrues on the loan from the time the loan is disbursed until it's paid in full.
- You can pay the interest while you're in school or during a period of deferment or forbearance.
- Or, you can allow the interest to accrue (accumulate) and have the interest added to the principal amount of your loan. If you choose not to pay the interest as it accrues and allow it to be capitalized, this will increase the total amount that you have to repay because you will be charged interest on a higher principal amount.

PLUS Loans (Direct or FFEL) are loans parents can obtain to help pay the cost of education for their dependent undergraduate children. In addition, graduate and professional degree students may obtain PLUS Loans to help pay for their own education.

Fixed Rates for Loans First Disbursed on or After July 1, 2006

Loan Type	Grade Level	Program			
		Direct Loans		FFEL	
		7/1/2006 to 6/30/2008	7/1/2008 to 6/30/2009	7/1/2006 to 6/30/2008	7/1/2008 to 6/30/2009
Subsidized Loans	Undergraduate	6.80	6.00	6.80	6.00
	Graduate	6.80	6.80	6.80	6.80
Unsubsidized Loans	Undergraduate	6.80	6.80	6.80	6.80
	Graduate	6.80	6.80	6.80	6.80
PLUS Loans	All	7.90	7.90	8.50	8.50

In addition to the interest rate, for all Direct Subsidized Loans and Direct Unsubsidized Loans first disbursed on or after July 1, 2007 and before July 1, 2008, there is also a loan fee (also called origination fee) of 2.5 percent.

The Direct PLUS loan fee is 4 percent for Direct PLUS Loans made to both parent and graduate and professional degree student borrowers.

For FFEL Loans the borrower may be charged fees comparable to the fees charged for Direct Loans, depending on the lender.

Private (Alternative) Student Loans

Private Education Loans, also known as Alternative Education Loans, are offered by private lenders and there are no federal forms to complete. Eligibility for private student loans often depends on the borrower's or cosigner's credit score.

Some families turn to private education loans when the federal loans don't provide enough money or when they need more flexible repayment options. For example, a parent might want to defer repayment until the student graduates, an option that is not available from the government parent loan program. (Many PLUS loan providers are

starting to allow parents to defer payments on the PLUS loan while the student is in school using an administrative forbearance. Interest continues to accrue, however.)

Private education loans tend to cost more than the education loans offered by the federal government, but are less expensive than credit card debt. The federal education loans offer fixed interest rates that are lower than the variable rates offered by most private student loans. Federal education loans also offer better repayment and forgiveness options. Private student loans typically have variable interest rates, with the interest rate pegged to an index, such as LIBOR or PRIME, plus a margin.

Private student loans may be used to pay for the EFC, the family's portion of college costs. While some lenders may offer private student loans in excess of the cost of attendance, any amount exceeding the difference between cost of attendance and financial aid is considered a resource. Like an outside scholarship, this will reduce need-based aid. Lenders provide different types of private education loans depending on the student's level of study.