



For Immediate Release
February 13, 2006

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Students' costs may be manageable even with passage of S 1932 TG projects up to \$5 monthly increase for student loan borrowers

ROUND ROCK, TEXAS – On Feb. 1, 2006, Congress passed S 1932 – The Deficit Reduction Act of 2005 – which included the Higher Education Reconciliation Act of 2005. Included in the legislation are two student loan interest rate changes which have been reported as dramatically increasing the cost of federal student loans to borrowers. The Congressional Budget Office (CBO) has estimated that these changes in borrower interest rates, in combination with maintaining the variable interest rate formula for lenders, will result in a \$15 billion savings to the federal government over a five-year period and \$36.3 billion savings through 2015.

To get a better picture of how these changes will affect individual student loan borrowers, TG – a nonprofit student loan guarantor that assists more than 550,000 parent and student borrowers each year – conducted a preliminary analysis of the impact on TG FFELP borrowers.

“We wanted to examine the actual impact of this one policy change because of its potential impact to students and families,” said George Torres, TG assistant vice president for congressional and legislative relations. “However, we certainly are not meaning to increase or diminish the impact of the policy choice of reducing borrower benefits as a method to control the cost of entitlement programs.”

Stafford Loan Interest Rate

The first “change” that TG examined was actually placed in the Higher Education Act in 2001. Congress chose to leave this scheduled change in place with this reconciliation bill. In effect, the Stafford loan interest rate will change from a variable interest rate (indexed from the three-month Treasury bill rate plus 1.7 percent while the borrower is in school or in grace, and 2.3 percent when the borrower enters repayment), to a fixed 6.8 percent interest rate for the life of the loan.

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Over the past few years, the Treasury bill rates have been at record lows, resulting in extremely low interest rates on Stafford loans. For the period of July 1, 2005, through June 30, 2006, the rate on these loans is 4.7 percent while a borrower is in school or in grace and 5.3 percent when the borrower enters repayment.

However, Treasury Bill interest rates have been going up since July 1, 2005. According to the CBO estimates, if the current rules remained in effect, and the rate stayed variable, it would increase to 6.2 percent while the borrower is in school and 6.8 percent when the borrower enters repayment on July 1, 2006. Also, this rate could continue in future years to increase up to the statutory cap of 8.25 percent.

The main difference between the old and new rules for student borrowers is the amount of interest that is capitalized into their loan value while they are in school. Under the old rules, this rate would be 6.2 percent during 2007, while it will be 6.8 percent under the new rules. For a student who enters a bachelor's degree program in the fall of 2006 and borrows the aggregate limit of Stafford loan funds (all unsubsidized) over a five-year period (for a total of \$23,000), this will result in \$436 dollars of additional debt when the student enters repayment. This translates into a \$5 month increase in loan payments (from \$255 to \$259 month) and a total cost of \$602 over the life of a 10-year loan.

PLUS Loan Interest Rate

The second interest rate change contained in the bill applies to PLUS loans (loans taken out by parents on behalf of their children). Under the current rules, this rate would have been fixed at 7.9 percent beginning July 1, 2006. With the enactment of S 1932, this rate changes to 8.5 percent. This translates into an additional cost of \$382 for every \$10,000 borrowed by parents under the PLUS Loan Program.

“It’s important to note that while there may be some additional cost, funds are still available,” said Torres. “The possible increase in cost should not act as a barrier to students enrolling in higher education.”

TG’s public service Web site, www.AIE.org, provides a loan repayment calculator that can help borrowers determine how their payments may be affected by the interest rate changes on July 1. In addition TG’s financial aid experts are available by phone at (800) 845-6267 to address borrowers’ concerns or answer specific questions about planning and paying for college.