Analysis of the Student Aid and Fiscal Responsibility Act of 2009

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Abstract

The Student Aid and Fiscal Responsibility Act of 2009 is a comprehensive piece of legislation focused on improving access to higher education. This policy analysis gives an overview of the specifics of the legislation, but is focuses on the proposed restructuring of the federal student loan system. The debate over and decision to implement a national direct loan program has the ability to revolutionize higher education and the American financial aid system for years to come.

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On September 17, 2009 the House of Representatives passed the Student Aid and Fiscal Responsibility Act. President Barack Obama set a national goal of having the highest proportion of college graduates worldwide by the year 2020 (Kruger, 2009). The president recognizes education as a gateway to producing a more informed and qualified public. The innovation and leadership required to achieve this goal demands restructuring the K-12 and post-secondary educational systems and subsystems that support the educational process. The Student Aid and Fiscal Responsibility Act is the Obama's administration proposed legislative policy to bring the 2020 vision to fruition. This landmark investment Act is a comprehensive attempt to reform the educational system from the initial stage of kindergarten through post secondary education. The early education aspect of the Act promotes early learning standards at the kindergarten and elementary levels with the optimism that these students will be more prepared to enter higher education institutions than their predecessors.

As previously stated, the Student Aid and Fiscal Responsibility Act has lofty ambitions with a "cradle to career" undertone. However, this analysis will focus on the proposed restructuring of the federal student loan system aspect of the legislation. The analysis begins with an overview of the various components of the Act and further explains the anticipated changes in the federal student loan system. Parson's policy process and Hogwood and Gunn's "Policy Analysis for the Real Word" provide a theoretical backdrop for analyzing the federal student loan system restructuring policy (1984). The policy issues are defined according to the both the proponent and opponent perspectives followed by a policy forecasting from each viewpoint. In the remaining sections of this paper, I provide an analysis of the relevancy of the policy followed by personal insight.

Policy Overview

In order to produce more college graduates, the Act promises to provide additional funding to Historically Black Colleges and Universities and Minority-Serving institutions, simplify the Free Application for Federal Student Aid (FAFSA) form, restructure the student lending system, and increase Pell Grant funding. Although the legislation is founded upon good intentions, it is not without controversy (Kruger, 2009). The Act proposes a change in the federal student loan system by implementing a system-wide Direct Loan (DL) program instead of allowing higher educational institutions to self-select between using the Federal Family Education Loan Program (FFELP) or the DL program (Kruger, 2009).

The Federal Family Education Loan Program allows private lenders to compete for customers, which can be students themselves or their parents. The current FFELP program offers four distinctive credit packages, Stafford loans, unsubsidized Stafford loan, federal Plus loans, and federal consolidated loans (Kruger, 2009). The federal government determines the interest rates on each of these loans. Moreover, when a private lender cannot secure sufficient capital to offer loans to borrowers the government provides subsidies to that particular institution. In contrast to FFELP, through the DL program students borrow directly from the federal government. The major policy debate lies in the government questioning the efficiency of the current amount of taxpayer dollars used to provide funds to private lenders.

Policy Objectives

The objective of the entire legislation is to provide greater access to higher education especially among under-represented groups in terms of ethnic identity and economic standing, therefore, making the opportunity to pursue higher education viable to anyone with the desire to attend. More specifically, the DL portion of the policy can be characterized as a redistributive policy because it uses reallocated funds from private lenders to finance need-based federal aid. In terms of efficiency, the DL proposal corrects market imperfections by implementing a system that reassures borrowers that their loans are not susceptible to the fallouts of the financial industry.

The credit crisis of 2007 made it difficult for non-bank lenders to secure sufficient capitol to provide loans to students. Borrowing from the U.S. Department of Education became a solution for many private lenders. Approximately 68 % of student loans were financed with Department of Education dollars. Opting to select a DL program would enable students, the end consumer, to borrow directly from the government (http://www.finaid.org). The instability in the external environment caused unpredictable changes in student lending that could have subsequently led to student drop-out. These unforeseen challenges in the credit industry served as a catalyst to ensure student loan availability. By lending to the students and not financial institutions, government leaders are predicting to enhance the public good by contributing to the education of the neediest students by guaranteeing financial assistance to students and not contributing to the profit or loss of private entities.

In contrast, the DL program allows the borrower to secure funds from the federal government and private lenders will bid on government contracts to service the loan. Servicing is defined as private lenders providing borrowers with information to prevent loan defaults. The new structure will allow lenders to provide back-end services instead of originating the initial loans with students.

Analysis

Access to post-secondary education is the core thematic issue of the Student Aid and Fiscal Responsibility Act, and the current federal student loan system is acknowledged as a barrier to entry and completion of post-secondary education for far too many students. According to Parson's policy process cycle, the direct loan policy is in the "evaluation of options" phase (Kivisto, 2009). If the DL program is selected as the new model for the federal loan system, the policy will move toward the implementation phase. Defining the problem of an issue determines how the policy will be reviewed; therefore, discussion of how the various stakeholders view the problem is required (Hogwood & Gunn, 1984).

There are two competing perspectives from government and the private sector that describe the flaws of student loan system very differently. According to interpretations of the legislation, the Obama administration views the unethical financial practices of private lenders as problematic and an impediment to the overall system. Furthermore, the government provides subsidies to private lenders to ensure the vitality of the student loan system, in order to protect the industry and students that depend on loans for educational expenses. Proponents of the DL program argue that the use of government subsidies for private lenders is a form of inefficiency and can be redirected to the other divisions of the federal financial aid program. According to the government's viewpoint, private lending corporations make profits with the use of public money. The government is projecting to use these funds to dedicate more money to the Pell Grant program, which assists low-income individuals.

On the other hand, lenders may define the major problem associated with the current federal student loan system as borrower default. Private lenders could argue that a borrower's inability to repay the loans in a timely manner as the root cause of insufficient funds to circulate cash flow within the system. It is even logical that private lenders may disassociate themselves as contributors to the ills of the student loan system and view these tribulations as a direct result of the increasing cost established by higher education institutions and the inability of students to afford these expenses.

Beyond defining the issue, forecasting from each perspective is a vital aspect of analyzing public policy (Hogwood & Gunn, 1984). The DL program is projected to save the government $87 billion dollars over the next 10 years, which will be reinvested in other government sponsored financial aid programs, such as the Pell Grant program. Opponents of the DL program anticipate that the government will actually cause the private lending sector to collapse thereby creating more economic woes in the form of job loss to the tune of approximately 10,000 jobs (Brown, 2009). The forecasting process in itself is highly politicized and based on the perspective of the stakeholder’s interest.

The legislation clearly states that it “proposes” a transition from FFELP loans to DL, which means that further investigation of the proposal is required for officials to make an informed choice. The term “propose,” which is stated in the official legislation does not connotate that any further action will take place. Merely proposing the idea does not guarantee that the plan will be implemented nor does it delineate a further course of action. Now that the legislation has been approved, it is the Obama administration’s responsibility to provide the public with an outline as to how the DL program will operate. The proposed savings are enormous, almost too good to be true.

The intent of the entire Student Aid and Fiscal Responsibility Act is to improve access to higher education. In a press conference hosted by The New American Foundation, Robert Shireman, deputy undersecretary for the Department of Education and representative of the

Obama administration, reported that his office has indentified low-income individuals as a source of untapped talent and possible new entrants to the higher education system (Brown, 2009). Therefore more money is needed for the Pell Grant program, which provides need-based aid to low-income individuals. The extra funding for the Pell Grant program can be generated through implementation of a system-wide DL program.

While the DL program may benefit 30% of the student population through more aid, it does not aid the majority of students that do not qualify for a Pell Grant (Brown, 2009). If providing access and aid to the masses is a national priority, then the eligibility requirements of the Pell Grant must be extended to encompass more recipients. Giving more financial assistance to fewer people does not help the whole. DL literature fails to prove how the average student will benefit from the switch over. During my initial research, I was under the impression that students would pay lower interest rates based on a testimony given before the House of Representatives (Altimire, 2009). However, that is not entirely factual, the interest rates will remain the same despite differences in the lending agency. If students still pay the same amount to borrow money, then the current cycle will persist.

DL literature also fails to inform the public about the cost of the program. Does the federal government have the capacity in both human and financial resources to undertake a feat such as administering loans for all of the nation's students? It cannot be assumed that the projected $87 billion dollars over the next ten years in savings is a net profit. The projected unforeseen costs are also not listed. For example, the certainty of the private lending market will be questionable without government subsidies. Also, the cost of hiring on private contractors from the lending industry is undefined.

Both proponents and opponents assume that borrowers default on loans because of a lack of financial literacy. This hypothesis overlooks the fact that borrowers simply may not be able to afford to repay the loans. The more appropriate debate should be entitled, "how do we control the cost of college?" True there are flaws within the student lending system, but at the rate at which college costs increase borrowers will incur debt that is proportional if not greater than the current debt/cost ratio.

While the Obama administration is open to exploring alternatives, the next dialogue should include government officials and higher education leaders regarding effective strategies to control college costs, only then will access truly improve.

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