Date of Hearing: June 19, 2012

ASSEMBLY COMMITTEE ON HIGHER EDUCATION
Marty Block, Chair
SB 1289 (Corbett) – As Amended: May 3, 2012

SENATE VOTE: 25-11

SUBJECT: Postsecondary education: private student loans.

SUMMARY: Requires a public, private, or independent postsecondary educational institution, except the California Community Colleges (CCC), to make specified disclosures related to private student loans in financial aid material and private loan applications provided or made available by the institution. Specifically, this bill:

1) Requires that a public, private, or independent postsecondary educational institution, except CCC, shall state all of the following in all printed and online financial aid materials issued or distributed by the institution to applicants for admission or matriculated students and with private loan applications provided or made available by the institution:

   a) Private loans lack flexible repayment options and borrower protections that federal loans are required to provide,

   b) Private loans may cost more than federal loans, and,

   c) Federal direct loans are available to students regardless of income.

2) Requires that institutions clearly distinguish private loans from federal loans in individual financial aid awards by stating, for any private loans included by the institution as part of the institution's award package, all of the following:

   a) Whether the rate is fixed or variable,

   b) An explanation that private loan interest rates may be higher than federal loan interest rates and may increase over time through no fault of the borrower,

   c) That there is no legal limit to the interest rate that borrowers may be charged on private loans,

   d) Any and all fees associated with the assumption of the loan, and,

   e) An explanation that the interest rate on a private loan may depend on the borrower's credit rating.

3) Requires that, if the institution provides a private loan lender list, it also shall provide general information on the terms of the loan available through the lender and disclose the reason for each lender's inclusion on the list, as well as the student's right to choose other lenders.

4) Requests that the CCC comply with the provisions of this legislation.

5) Clarifies that the provisions of this legislation apply to the University of California (UC) only to the extent that the provisions are adopted by the UC Regents through a resolution.

EXISTING LAW: Several programs for student loans have been established under federal law through the William D. Ford Direct Loan Program, which is operated by the U.S. Department of Education's Federal Student Aid Office. These loan programs include:

1) Subsidized Stafford Loans: These are needs-based loans that cover the difference between a student's resources and the cost of attending a college or university; the amount of loan is dependent on the level of need, dependent status, and year in college. The federal government pays the interest while the student is attending the college or university and subsidizes the interest throughout the life of the loan.

2) Unsubsidized Stafford Loans: Not based on financial need, these loans generally cover the difference between the subsidized Stafford Loan and the total cost of attending college. Loans are made by private lending institutions and repayment is guaranteed by the federal government. The federal government sets the interest rates and fees.

3) PLUS (Parent Loans for Undergraduate Students): Available to creditworthy parents of dependent students. These are not needs-based and are federally guaranteed. In addition, these types of loans have been expanded for graduate or professional degree students. The borrower is responsible for paying the interest on PLUS loans during all periods, starting from the date the loan is first disbursed.

Before July 1, 2010, Stafford, PLUS, and Consolidation Loans were also made by private lenders under the Federal Family Education Loan Program. As a result of the *Health Care and Education Reconciliation Act of 2010*, all new Stafford and PLUS Loans come directly from the Department of Education under the Direct Loan Program.

FISCAL EFFECT: The Senate Appropriations Committee determined that there was either no cost to the state or minimal costs, pursuant to Rule 28.8.

COMMENTS: Background. The cost of higher education has unquestionably increased over the last decade, forcing students to take out increasingly high levels of debt to finance their education. The College Board's Trends in Student Aid 2011 report notes that over the decade from 2000-01 to 2010-11, undergraduate borrowing increased by 56% per full-time equivalent student. In California, cuts to public higher education institutions have had an impact on how students finance college and where they choose to attend school. In June 2012, the Public Policy Institute of California issued, *Defunding Higher Education*, which found that, from 2007-2011, fees at the California State University increased by 47% and by 50% at the University of California.

Federal vs. private loans. Students have two options when looking to take out loans – federal loans and private loans. Federal loans, like Stafford Direct Loans, have fixed rates with set caps, limits on fees, and flexible repayment options. While federal loans make up the majority of student loan borrowing, there are limits to how much money students can borrow under federal loan programs; the remaining "unmet need" to cover total educational expenses are often financed through private loans.

The Institute on College Access and Success (TICAS) writes in "Private Loans: Facts and Trends" that “private student loans are one of the riskiest ways to finance a college education.” According to TICAS, like credit cards, private student loans usually have variable interest rates that are higher for those who can least afford them – as high as 18% in 2008. But unlike credit card debt, these loans are nearly impossible to discharge in bankruptcy. Private student loan borrowers are also not eligible for the important deferment, income-based repayment, or loan forgiveness options that come with federal student loans.

According to the College Board’s Trends in Student Aid 2011, private loans, which are not part of the student aid system and do not involve subsidies, grew from $5.1 billion in 2000-01 to $22.1 billion in 2007-08. Since that year, student loan volume from banks, credit unions, and other private lenders has declined to $6 billion. The College Board also notes that, in 2009-10, nationwide about 55% of graduates from public four-year colleges graduated with debt, borrowing an average of $22,000. About two-thirds of those earning bachelor's degrees from private nonprofit institutions had debt averaging $28,100.

Need for this bill. According to the author, consumers, especially students without parental support and parents whose first child is headed to college, lack readily accessible and understandable information about the cost of a college education. They also lack unbiased, expert advice on the best way to borrow money to finance their education. The author notes that Finaid.org reports that private student loan volume is expected to return to the 25% annual growth rate unless there is another increase in federal loan limits or an expansion of the availability of federal student loans. According to the author, if current trends continue, annual private education loan volume will surpass federal student loan volume by around 2030.

Federal disclosure requirements. In 2008 the federal government enacted the Higher Education Opportunity Act (HR 4137), which prohibits private education loans from being consummated before applicants submit a signed self-certification form that institutions of higher education provide to students. The private education loan self-certification form contains numerous disclosures, including information that free federal aid might available in addition to, or in the place of, a private education loan. This form also strongly encourages students to pursue free or lower-cost financial aid through an institution’s federal financial aid office. The private self-certification must also include the estimated total cost of attendance, the financial assistance for the period covered by the loan, and the difference between the total cost and estimated financial aid. Borrowers need to submit the self-certification prior to receiving a private or direct student loan.

Technical and clarifying amendments. This bill’s provisions are intended to provide disclosure about various loan options for prospective borrowers. Staff recommends the following technical and clarifying amendments:

a) On page 2, lines 14-15, strike the current language and instead insert: “Federal student loans are required by law to provide a range of flexible repayment options, such as income-based repayment and income-contingent repayment plans, loan forgiveness benefits, and borrower protections that private student loans are not required to provide.”

b) On page 2 line 16, after “more” insert “or less”

c) On page 2 lines 30-33, clarify the variability of private loans.

d) On page 2 between lines 33 and 34, insert, "(3) Students should contact the lender of the private student loan or their educational institution's financial aid office if they have questions."

e) On page 3 lines 5-7, amend to read, "…disclose the ~~reason~~ basis for each lender's inclusion on the list. The institution shall also ~~inform~~ disclose in the list that the student ~~of his or her right~~ has the ability to choose ~~other~~ any lenders."

Arguments in support. The California Student Aid Commission writes that, "SB 1289 is consistent with our Commission's program principal to provide information and guidance to students and their families on alternative methods for financing a college education. Last year student loan debt surpassed credit card debt, and private student loans are an ever-increasing proportion of that number."

The American Federation of State, County, and Municipal Employees (AFSCME) writes that, "students often are not aware that some private loans don't have the same protections as federal loans, have uncapped variable interest rates, and lack flexible repayment options. SB 1289 is an important bill that provides private student loan information upfront so that students and their families can make fully informed decisions on the best way to fund their educations."

Arguments in opposition. The California Association of Private Postsecondary Schools writes that, "under current law, including the Truth in Lending Act (TILA) and the United States Department of Education financial aid regulations (FSA), schools and financial institutions are already required to provide extensive disclosures to prospective borrowers. The existing disclosures provide the same sort of disclosures mandated under SB 1289."

REGISTERED SUPPORT / OPPOSITION:

Support

American Federation of State, County and Municipal Employees
Associated Students of the University of California, Davis
California Faculty Association
California Student Aid Commission
Consumer Federation of California
Institute for College Access & Success
Public Advocates, Inc.
University of California Student Association
Western Association for College Admission Counseling

Opposition

California Association of Private Postsecondary Schools

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