STATEMENT OF

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before the

Subcommittee on Postsecondary Education
Committee on Education and Labor
U.S. House of Representatives

March 10, 1982

There should be no release
of this document before its
delivery, scheduled for 9:00 a.m.
Wednesday, March 10, 1982.

Mr. Chairman, the federal government currently helps finance the education of about half of all postsecondary students through grants, direct and guaranteed loans, and work-study aid. In fiscal year 1981, outlays under all such programs totaled $10.2 billion. If one counts the full principal value of student loans, all of jointly funded work-study programs, and direct grants, the total amount of federally supported aid in 1981 approached $15 billion. This aid accounted for about one-third of all student expenses for tuition and room and board, and represented about three-quarters of all student assistance provided by governments and educational institutions.

Although precise information is unavailable, it appears that between 5 and 6 million postsecondary students received some federal assistance in 1981. About 2.6 million students received Pell grants, 3.5 million borrowed under the Guaranteed Student Loan (GSL) program, between 1 and 2 million were assisted through the campus-based programs, and 650,000 received Social Security postsecondary student benefits. The number obtaining aid under more than one program is not known, however.

Undergraduates receive aid under all programs, whereas graduate and professional students are assisted almost exclusively through the GSL program. Students at private institutions receive a disproportionately large share of total aid, principally because their higher expenses qualify them for larger GSLs.

My remarks today will cover three topics:

- o Recent trends in federal student assistance;
- o Last year's funding actions; and
- o The Administration's 1983 proposals, as well as other alternatives available to the Congress.

RECENT TRENDS

Over the last decade, the amount of federal student assistance grew rapidly, while the mix of aid and the types of students assisted changed as well. Throughout the early and middle 1970s, the great majority of aid was provided either through grants and work-study assistance targeted primarily on disadvantaged students or through educational benefits for veterans. Between 1970 and 1978, federal outlays more than tripled and total assistance grew from $2.8 billion to $8.7 billion (see Table 1).

The passage of the Middle Income Student Assistance Act (MISAA) in 1978 and subsequent legislative actions increased the amount of student assistance dramatically--especially for middle- and upper-income students--and shifted the composition of aid heavily toward loans. Between 1978 and 1981, total available aid grew by 70 percent, to $14.7 billion. Almost half of all aid in 1981 was in the form of loans--up from one-quarter in 1978. The growth of the GSL program also meant that roughly 20 percent of all aid in 1981 went to students from families with incomes over $30,000, whereas little aid had gone to comparable students before 1978.

TABLE 1. FEDERAL POSTSECONDARY STUDENT ASSISTANCE, FISCAL YEARS 1970-1982 (In billions of dollars)

	1970[a]	1978	1979	1980	1981	1982[b]
Federal Spending (Outlays)	1.9	7.1	7.6	8.7	10.2	9.4
Total Federally Financed Aid[c]	2.8	8.7	9.8	11.7	14.7	14.3
Loan volume[d]						
GSLs	0.8	1.7	2.5	3.9	6.3	7.3
NDSLs	0.4	0.4	0.7	0.7	0.8	0.6
Total	1.2	2.1	3.2	4.6	7.1	7.9
Outlays for grants and work-study aid[e]						
Pell grants	--	1.6	1.8	2.4	2.5	2.3
SSIG and SEOG	0.2	0.3	0.3	0.4	0.5	0.4
Work-study aid	0.2	0.5	0.7	0.7	0.7	0.7
Social Security benefits	0.4	1.4	1.5	1.7	2.0	1.4
Veterans' benefits	0.8	2.8	2.3	1.9	1.9	1.6
Total	1.6	6.6	6.6	7.1	7.6	6.4

a. Obligations, rather than outlays, were used for the GSL, National Direct Student Loan (NDSL), Supplemental Educational Opportunity Grant (SEOG), and work-study programs for 1970.

b. Estimated.

c. Total aid includes the principal value of loans and all aid provided by programs that require matching funds from institutions.

d. Assumes that one-half of GSLs obtained in each fiscal year is used for education during the following year. NDSL loan volume includes that financed by federal spending, by institutional matching funds, and by capital in the revolving account.

e. Assumes that available aid equals federal outlays plus institutional work-study matching funds.

LAST YEAR'S ACTIONS

Last year, the Congress took a number of actions to reduce student aid programs. These changes included: requiring a "needs analysis" for GSL borrowers from families with incomes above \$30,000; establishing a 5 percent GSL origination fee; phasing out Social Security benefits for postsecondary students; reducing all Pell grant awards; and cutting appropriations for other student assistance programs. Together, these changes are expected to reduce 1983 outlays by \$3.2 billion, or 25 percent, below projected outlays without the changes. Available aid in 1983 will be lower by \$5 billion, or almost 30 percent.

One major effect of last year's actions will be to eliminate or reduce GSLs for 1 million students with family incomes greater than \$30,000. Although this is not likely to affect the access of these students to continued education, they may now choose less expensive institutions. Second, Pell grant awards will fall by \$80 for 2.6 million students; virtually all of these students have family incomes below \$30,000, and three-fourths have incomes below \$20,000. Third, the 1983 cuts in Social Security benefits will average \$2,500 for about 650,000 students, many of whom are from low-income families. Although Pell grants will partially offset these cuts, the extent is uncertain.

THE ADMINISTRATION'S PROPOSALS AND ALTERNATIVES

In its 1983 budget submission, the Administration has proposed further reductions in the GSL, Pell grant, and campus-based student assistance programs. The CBO estimates that, compared with current policies, these proposals would reduce federal spending by 10 percent and available aid by 15 percent in 1983. The reductions would grow over time--to 30 percent and 40 percent, respectively, in 1984 (see Table 2).

GSL Proposals and Alternatives

The Administration is proposing several further reductions in the GSL program. Two proposed changes would limit eligibility for GSLs: first, by extending the needs analysis to all students; and second, by making all graduate and professional students ineligible for the GSL program. Two other changes would reduce the subsidy for those who remained eligible: first, by increasing the loan origination fee to 10 percent; and second, by requiring that new borrowers pay market interest rates on their loans beginning two years after they leave school. The CBO estimates that together these proposals would reduce federal spending for GSLs by \$200 million in 1983, and by \$4.1 billion over the next five years. The volume of new loans would decline by \$1.4 billion, or about 20 percent, in 1983.

TABLE 2. COMPARISON OF FEDERAL SECONDARY STUDENT ASSISTANCE UNDER CURRENT POLICIES AND ADMINISTRATION PROPOSALS, FISCAL YEARS 1982-1984 (In billions of dollars)

	1982	1983		1984	
	Current Policies	Current Policies	Administration Proposal	Current Policies	Administration Proposal
Federal Spending (Outlays)	9.4	9.0	8.4	9.2	6.7
Total Federally Financed Aid[a]	14.3	12.7	10.9	12.4	7.7
Loan volume[b]					
GSLs	7.3	6.8	5.4	6.8	4.1
NDSLs	0.6	0.6	0.6	0.7	0.5
Total	7.9	7.4	6.0	7.5	4.6
Outlays for grants and work-study aid[c]					
Pell grants	2.3	2.3	2.0	2.5	1.3
SSIG and SEOG	0.4	0.3	0.3	0.4	---
Work-study aid	0.7	0.7	0.6	0.7	0.5
Social Security benefits	1.4	0.8	0.8	0.4	0.4
Veterans' benefits	1.6	1.2	1.2	0.9	0.9
Total	6.4	5.3	4.9	4.9	3.1

a. Total aid includes the principal value of loans and all aid provided by programs that require matching funds from institutions.

b. Assumes that one-half of GSLs obtained in each fiscal year is used for education during the following year. NDSL loan volume includes that financed by institutional matching funds and by capital in the revolving account.

c. Assumes that available aid equals federal outlays plus institutional work-study matching funds.

Taken together, the Administration's GSL proposals would eliminate large numbers of currently eligible borrowers while only moderately reducing the subsidy available to those who could still qualify. The risk associated with this approach is that those made ineligible would be unable to obtain other loans and would, thereby, be denied access to continued education or would have to attend less-costly institutions. Although graduate and professional students would be permitted to borrow under the much less subsidized Auxiliary Loan Program, states have been slow to implement it, so the risk of decreased access would remain.

Other approaches are available that would reduce GSL expenditures while eliminating fewer persons from the program. Specific alternatives include increasing students' borrowing costs (either for all borrowers or only for certain groups, such as those who would be made ineligible under the Administration's proposal) and decreasing lenders' yields. Alternatively, the Congress could end the entitlement status of the program--which would make costs easier to control but might also limit some students' access to continued education.

Increasing Students' Borrowing Costs. The Congress could lower students' subsidies while continuing to allow them to borrow, either by ending federal payment of interest on the loans while the students are in school or by raising the interest rates charged on loans.

Eliminating "in-school" interest payments would reduce the present value of borrowers' subsidies--and, therefore, long-term federal expenditures--by half. This option could be designed so that students would not have to make any interest payments while in school. Depending on how it was structured, such a change could reduce federal GSL costs by up to $4 billion during the next five years if applied to all borrowers, or up to $1.6 billion if applied only to those who would be made ineligible under the Administration's proposal.

Another alternative would be to raise students' interest rates. At present, most borrowers are charged 9 percent on their loans, while persons who took out their first loans before January 1981 may continue to borrow at 7 percent interest. Both these rates provide large interest subsidies that were not available when the program was initiated in 1965. Although near-term savings from raising students' interest rates would be small because the change would affect federal outlays only after students leave school, eventual savings would be substantial. Each one-percentage-point increase in the rate charged on all new loans would reduce federal spending by $100 million during the next five years alone if applied to all borrowers.

Reducing Lenders' Yields. Another approach would be to lower lenders' yields on all new loans--from the current level of 3.5 percentage points above the bond-equivalency rate on 91-day Treasury bills. Many persons have argued that the current yield provides a larger return than necessary to induce lender participation in the program, given present servicing costs and the value to lenders of a fully indexed and guaranteed return in times of highly variable interest rates. Although substantial cuts in yields might drive some lenders out of the program, smaller decreases would carry less risk. This risk could be further reduced by lowering lenders' yields in steps--with the lowest yield paid to those with the largest volume, thereby taking account of lenders' economies of scale. Although early savings under this option would be quite small, each one-percentage-point decrease in average yields on new loans could save $600 million over the next five years.

Restricting Loan Volume. A third approach to reducing GSL costs would be to restrict the dollar volume of loans made each year--that is, to end the entitlement status of the program. Although capping loan volume would provide perhaps the simplest means of limiting program growth, it is not clear how available funds would be rationed among states or institutions. Moreover, unless constrained, lenders might choose to provide loans only to their best customers, who would generally not be the most needy students. The number of students eliminated under this option--and the federal savings--would depend on the level at which the cap were set.

Pell Grant Proposals and Alternatives

In the Pell grant program, which serves lower-income students, the Administration is proposing to rescind a small amount of 1982 funding and to reduce 1983 funding to $1.4 billion--40 percent below the present 1982 appropriation. The Administration is proposing to achieve the 1983 savings, in part, by reducing the maximum award from $1,800 to $1,600, and, in part, by reducing the number of eligible students by 800,000 Achieving the total proposed savings would mean reducing the average award from about $1,300 to $800 for the 1.8 million students who would remain eligible. A student from a family of four whose total income is $15,000, for example, would receive about $500 rather than $1,000.

While other options for reducing Pell grants are available, if the Congress chooses to cut spending by 40 percent, as requested by the Administration, awards would have to be substantially reduced for large numbers of low-income students. Alternatively, if spending for Pell grants is to be cut less, but the total reduction in financial aid proposed by the Administration is to be achieved, greater savings would have to be found in other programs such as GSLs.

Other Proposals and Alternatives

Finally, the Administration is proposing to eliminate several other student assistance programs and to reduce funding for the remaining ones. Specific proposals include: abolishing the State Student Incentive Grants (SSIGs) and Supplemental Educational Opportunity Grants (SEOGs), providing no new capital contributions for National Direct Student Loans (NDSLs), and reducing work-study funds by about 25 percent from their 1982 appropriation level. Together, these proposals would reduce aid under these programs from $1.7 billion in 1982 to $1.5 billion in 1983 and to $1 billion in 1984.

Because these programs principally serve less-well-off students, the proposed reductions would also fall on that group. The specific impacts, however, would depend on how institutions chose to distribute the funds that remained. The Congress could lessen the impacts of these cuts on those most in need by limiting the use of remaining funds or by requiring that institutions provide a greater proportion of matching funds.

CONCLUSIONS

In summary, federal student aid has expanded rapidly since 1970, with much of the recent growth occurring in loans for middle- and upper-income students. Last year, the Congress slowed this growth by curtailing loans for higher-income students and reducing grants for a sizable number of low-income students. If the Congress chooses to reduce outlays further this year, the challenge will be to target reductions in aid on those who least need it and to limit the risk of denying students' access to continued education.