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Bringing Market Forces to the Loan Program

By STEPHEN BURD

The U.S. Education Department and the General Accounting Office have released a draft report that identifies five possible models for injecting market forces into the guaranteed-student-loan program.

The report does not endorse any of the models, and members of the panel whose study led to the report have expressed little enthusiasm for them. "I haven't seen any evidence that these options would provide significant-enough savings for students or taxpayers to warrant any major changes," said Corye Barbour, legislative director for the United States Student Association, and a panel member.

In 1998, lawmakers drafting a new version of the federal Higher Education Act asked why it is up to Congress to decide on the interest rate that borrowers should pay on their loans, and on the profit margin that banks should have in making the loans.

With that in mind, Congress ordered the Education Department and the General Accounting Office, Congress's investigative arm, to convene a group to study the issue.

Since March, officials of the two agencies have led a study group made up of student-loan-industry officials, college lobbyists and administrators, and student advocates to find ways to improve the guaranteed-loan program by minimizing the government's role and maximizing the influence of the open market.

The five options that the panel identified are:

- * Adjustments to the current system: Under this model, the Education Department or a blue-ribbon commission would collect data from current market transactions to determine the appropriate level of "lender yield," or profit, which Congress or some independent entity would set.
- * Auctions: Lenders would bid for the right to originate student loans.
- * Loan sales: The federal government would make the loans and then sell them at auction to lenders, who would collect the payments and work to prevent borrowers from going into default.
- * Federal financing: Lenders would borrow funds from the federal government to make guaranteed loans.
- * Rates set by the market: Lenders and borrowers would negotiate their own interest rates and other terms. The process would set both the profits of lenders and the interest rates paid by borrowers.

A final report is due out by May 15.

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