CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

May 20, 2013

H.R. 1911
Smarter Solutions for Students Act

As ordered reported by the House Committee on Education and the Workforce on May 16, 2013

SUMMARY

H.R. 1911 would change the interest rates for all new federal loans to students and parents made on or after July 1, 2013, from a fixed interest rate set in statute to a variable interest rate, adjusted annually. Under the bill, interest rates for all new subsidized and unsubsidized student loans would be based on the interest rate on a 10-year Treasury note plus 2.5 percentage points, with a cap of 8.5 percent. (Borrowers pay no interest on subsidized loans while enrolled in school or during other deferment periods but are responsible for interest at all times on unsubsidized loans.) The interest rate for all new GradPLUS and parent loans would be based on the interest rate on a 10-year Treasury note plus 4.5 percentage points, with a cap of 10.5 percent. The bill also would eliminate the cap on the interest rate on all new consolidation loans (multiple loans for a single borrower combined into one loan) originated on or after July 1, 2013.

Under current law, all subsidized and unsubsidized loans originated on or after July 1, 2013, will have a fixed interest rate of 6.8 percent, and all GradPLUS and parent loans will have a fixed rate of 7.9 percent. In addition, the interest rate on all consolidation loans is capped at 8.25 percent.

CBO estimates that enacting H.R. 1911 would reduce direct spending by about $1.0 billion over the 2013-2018 period and by $3.7 billion over the 2013-2023 period. Enacting the bill would not affect revenues. Pay-as-you-go procedures apply because enacting the legislation would affect direct spending. Implementing the bill would not have a significant impact on spending subject to appropriation.

H.R. 1911 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R.1911 is shown in the following table. The costs of this legislation fall within budget function 500 (education, training, employment, and social services).

	By Fiscal Year, in Millions of Dollars												
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2013-2018	2013-2023
CHANGES IN DIRECT SPENDING													
Estimated Budget Authority	3,870	1,495	-1,815	-2,010	-1,690	-1,355	-1,000	-670	-420	-255	-145	-1,505	-3,995
Estimated Outlays	2,195	2,030	-565	-1,720	-1,610	-1,325	-1,020	-725	-480	-305	-195	-995	-3,720

BASIS OF ESTIMATE

As required under the Federal Credit Reform Act of 1990, most of the costs of the federal student loan programs are estimated on a net-present-value basis. Under credit reform, the present value of all loan-related cash flows is calculated by discounting those expected cash flows to the year of disbursement, using the rates for comparable maturities on U.S. Treasury borrowing. (For example, the cash flow for a one-year loan is discounted using the rate for a one-year zero-coupon Treasury note.) The costs for the federal administration of student loans are estimated on a cash basis. For this estimate, CBO assumes the bill will be enacted by July 1, 2013.

Background on Student Loans

The federal government currently administers four types of student loans:

- **Stafford subsidized loans**. Subsidized loans are available only to undergraduate students who demonstrate financial need. Borrowers pay no interest on those loans while they are enrolled in school or during other periods of deferment. The interest rate for subsidized loans is 3.4 percent for academic year 2012-2013 but is scheduled to rise under current law to 6.8 percent for academic year 2013-2014 and thereafter. The annual and aggregate amounts a student may borrow are limited by the borrower’s year in school and dependency status.

- **Stafford unsubsidized loans**. Unsubsidized loans are available to undergraduate and graduate students regardless of financial need. Borrowers are responsible for interest on those loans at all times. Under current law, the interest rate for subsidized loans is 6.8 percent and will remain 6.8 percent in the future. The annual and aggregate amounts a student may borrow are limited by the borrower's year in school, dependency status, and the amount borrowed under the subsidized loan program.

- **GradPLUS loans**. GradPLUS loans are loans specifically for graduate students who wish to borrow above the annual or aggregate limits on unsubsidized student loans. Under current law, the interest rate on GradPLUS loans is 7.9 percent and will remain so. Students may borrow up to the cost of attendance at their institution (minus any other financial aid received).

- **Parent loans**. Parent loans are available to parents of students. Under current law, the interest rate on PLUS loans is 7.9 percent and will remain so. Parents may borrow up to the cost of attendance at their institution (minus any other financial aid received).

In addition, under current law, borrowers with multiple loans can consolidate all of their loans into a single loan with a fixed interest rate. That rate is based on a weighted average of the rates of all loans that are consolidated, rounded up to the nearest one-eighth of one percent with a cap of 8.25 percent.

Direct Spending

Under H.R. 1911, the interest rate for all four types of loans would adjust annually based on the last auction of Treasury rates in May of each year for the upcoming academic year (July 1 through June 30). As of the date of this estimate, that auction for 2013 has not occurred. Accordingly, this estimate uses CBO's projection of the rate for the 10-year Treasury note in 2013. The estimated costs of the legislation would change once that auction has taken place and CBO knows what the actual rate for academic year 2013-2014 will be.

Under the bill, the interest rates for all new subsidized and unsubsidized student loans would be equal to the interest rate on the 10-year Treasury note plus 2.5 percentage points, with a cap of 8.5 percent. Including the effect of the cap of 8.5 percent, which lowers the expected value of future interest rates, CBO projects that interest rates for those loans would rise from about 5 percent for academic year 2014-2015 (below the fixed rate of 6.8 percent in current law) to about 7 percent for academic year 2023-2024.

Also under the bill, the interest rate for all new GradPLUS and parent loans would be based on the interest rate on a 10-year Treasury note plus 4.5 percentage points, with a cap of 10.5 percent. CBO projects that interest rates for those loans would rise from about 7 percent for academic year 2014-2015 (below the fixed rate of 7.9 percent in current law) to about 9 percent for academic year 2023-2024, which also includes the effect of the cap of 10.5 percent.

In addition, the bill would eliminate the cap of 8.25 percent on all consolidation loans originated as of July 1, 2013, regardless of when the initial loans being consolidated were originated.

CBO also projects that as interest rates rise above the level in current law, some borrowers, particularly those in the GradPLUS and parent loan programs, would reduce the amount of their federal borrowing. By 2023, CBO estimates that the volume in GradPLUS and parent loan programs would decline by about 15 percent under H.R. 1911.

Based on the changes in interest rates and loan volume, CBO estimates that enacting H.R. 1911 would increase direct spending by $2.2 billion in fiscal year 2013 and decrease direct spending by about $1.0 billion over the 2013-2018 period and by $3.7 billion over the 2013-2023 period.

PAY-AS-YOU-GO CONSIDERATIONS

The Statutory Pay-As-You-Go Act of 2010 establishes budget-reporting and enforcement procedures for legislation affecting direct spending or revenues. The net changes in outlays and revenues that are subject to those pay-as-you-go procedures are shown in the following table.

CBO Estimate of Pay-As-You-Go Effects for H.R. 1911 as ordered reported by the House Committee on Education and the Workforce on May 14, 2013

	By Fiscal Year, in Millions of Dollars												
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2013-2018	2013-2023
	NET INCREASE OR DECREASE (-) IN THE DEFICIT												
Statutory Pay-As-You-Go Impact	2,195	2,030	-565	-1,720	-1,610	-1,325	-1,020	-725	-480	-305	-195	-995	-3,720

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 1911 contains no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

ESTIMATE PREPARED BY:

Federal Costs: Deborah Kalcevic
Impact on State, Local, and Tribal Governments: J'nell L. Blanco
Impact on the Private Sector: Vi Nguyen

ESTIMATE APPROVED BY:

Peter H. Fontaine
Assistant Director for Budget Analysis