Student Loan Repayment

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POSTSECONDARY NATIONAL POLICY INSTITUTE

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Contents

Clicking the PNPI Logo at the top-right of each page will return you to this table of contents

Summary

The benefits of a college education are clear. The average bachelor's degree graduate earns $1.2 million more over the course of their career than the average high school graduate, although outcomes vary widely depending on course of study.[1] Still, postsecondary education can be very costly. Rising college costs over the last several decades have left most students and families turning to federal student loans to pay for college. Over six in ten bachelor's degree graduates left school with student loan debt in 2019 and 43 million Americans now hold federal student loans—up from 38 million in 2012.[2] There are several options for loan repayment; though most borrowers use the standard 10-year repayment plan, a majority of the outstanding student debt is held by borrowers who have plans based on their income. Those who fail to repay face delinquency or default, and one's likelihood of falling into delinquency or default varies by demographics and institutional sector. This primer documents how student loan borrowers can repay their loans and how federal repayment policies impact borrowers.

A Brief History of Federal Student Loans

The precursor to today's federal student loan program started under the Higher Education Act of 1965's Guaranteed Student Loan program, also known as the Federal Family Education Loan (FFEL) program. Under the FFEL program, ED encouraged private lenders to participate in the program by offering subsidies to those who participated. In addition to these subsidies, the government guaranteed that lenders would be compensated for a portion of their losses if a borrower defaulted. In 1993, Congress implemented the Direct Loan program, which allows students and their families to borrow directly from the federal government through ED with U.S. Treasury funds. With no lender subsidies to pay, this program reduced the government's cost of making a student loan.

For nearly 20 years, the Direct Loan and FFEL programs coexisted, with schools selecting which program to participate in and borrowers receiving nearly identical loan terms that were set in statute. In 2008, largely due to the credit crisis, several private lenders no longer found it feasible to participate in the FFEL program. To ensure the stability of the student loan market, ED offered to repurchase FFEL program loans from private lenders and absorb these loans into the Direct Loan program as part of the Ensuring Continued Access to Student Loans Act (ECASLA). These repurchased loans are referred to as "Department-held FFEL." In 2010, the Student Aid and Fiscal Responsibility Act (SAFRA) halted the availability of new FFEL program loans and mandated a complete switch to direct lending by June 30, 2010.[3] By June 2021, remaining FFEL program loans represented only 15% ($234.1 billion) of the $1.6 trillion in outstanding federal student loans. The remaining loan volume consisted of almost all Direct Loans ($1.35 trillion).[4]

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[1] See Carnevale et al. (2021).

[2] Based on TICAS (2020) & Federal Student Aid (2022).

[3] SAFRA was passed as part of the Health Care and Education Reconciliation Act of 2010 (P.L. 111-152), which President Obama signed into law on March 30, 2010. It terminated the authority to make loans under the Federal Family Education Loan (FFEL) program after June 2010. For more information, see the Congressional Research Service report.

[4] Perkins Loans totaled $4.7 billion. Institutions of Higher Education (IHEs) technically handle the servicing of Perkins Loans. However, some IHEs contract with outside entities.

Current Available Loan Options

There are four types of loans a current borrower may hold:

- A federal student loan made by ED under the William D. Ford Direct Loan Program (Direct Loan);
- A student loan previously issued under the Perkins Loan program;
- A student loan previously issued under the FFEL program guaranteed by the federal government (FFEL loans); and
- A private student loan that is issued and serviced by an entity outside of the Direct Loan or FFEL program.

Within the Direct Loan program, students and their families can have either a Subsidized or Unsubsidized Direct Loan, a Parent PLUS Loan, a Grad PLUS Loan, or a Consolidation Loan.[5] Consolidation allows borrowers to combine multiple federal student loans into one loan with one monthly payment, typically at a lower monthly payment but over a longer repayment term. FFEL loans are no longer issued; any holders of these loans received them before SAFRA went into effect.

In order to obtain and pay off a Direct Loan, the student or their family must complete several steps, beginning with the Free Application for Federal Student Aid (FAFSA). Table 1 details the steps in the life of a Direct Loan.

Table 1: Steps in the Life of a Direct Loan

1	Borrower submits completed **FAFSA,** and the **Student Aid Report** (including Expected Family Contribution) is generated.
2	Schools listed on the borrower's FAFSA send **financial aid packages**, which may include Direct Loans, to the borrower.
3	Borrower accepts the school's admission offer and financial aid award, including the Direct Loan, by signing the **promissory note**.
4	After the borrower completes **entrance counseling**, the school disburses the Direct Loan. The borrower's loan status is "**In School.**"
5	Once the borrower leaves school (or drops below half-time enrollment), the borrower's loan status is "**In Grace.**" The borrower has **exit counseling**.
6	Once the grace period ends, the Direct Loan becomes "**In Repayment,**" unless the loan servicer approves a deferment or forbearance.
7	Under the **standard repayment plan**, the borrower will pay back the Direct Loan in 10-year equal installment payments. **Income-based repayment** plans offer longer terms, and **loan forgiveness** is available to qualified borrowers. During repayment, the borrower will work with an assigned federal loan servicer.
8	If the borrower fails to make payments for 360 days, the borrower is considered "**In Default**" and the Direct Loan is transferred to **debt collection**.

Adapted from the glossary available at https://studentaid.gov/sa/glossary.

[5] For more information on types of student aid, please see PNPI's Federal Student Aid Primer.

ED refers to a loan's status to determine where a student loan is in the repayment process. Table 2 details key student loan statuses.

Table 2: Definitions of Key Student Loan Statuses

Loan Status	Definition
Default	Failure to repay a loan according to the terms agreed to in the promissory note. For most federal student loans, borrowers will default if they have not made a payment in more than 270 days. However, FSA generally identifies defaulted loans as those that are 360 days or more past due, because loan servicers have additional time to transfer Direct Loans to FSA's Debt Management & Collections System.
Deferment	A postponement of payment on a loan that is allowed under certain conditions and during which interest does not accrue on Direct Subsidized Loans, Subsidized Federal Stafford Loans, and Federal Perkins Loans. All other federal student loans that are deferred will continue to accrue interest. The most common type of deferment is for borrowers enrolled in school, but borrowers can also receive deferments if they are experiencing a period of economic hardship or active military duty. Any unpaid interest accrued during the deferment period may be added to the principal balance (capitalized) of the loan(s).
Delinquent	A loan is delinquent when loan payments are not received by the due dates. A loan remains delinquent until the borrower makes up the missed payment(s) through payment, deferment, or forbearance.
Forbearance	A period during which monthly loan payments are temporarily suspended or reduced. Forbearance may be granted to borrowers willing but unable to make loan payments due to certain types of financial hardships. Also, borrowers applying for an income-based repayment plan are placed on administrative forbearance. During forbearance, principal payments are postponed but interest continues to accrue. Unpaid interest that accrues during the forbearance will be added to the principal balance (capitalized) of loan(s), increasing the total amount owed.
Grace Period	The period of time after the borrowers graduate, leave school, or drop below half-time enrollment where they are not required to make payments on certain federal loans. Six months is the standard grace period. Some federal student loans will accrue interest during the grace period, and if the interest is unpaid, it will be added to the principal balance of the loan when the repayment period begins.
Repayment	Following the grace period, borrowers pay off the balance of their loans. Borrowers may select one of several predefined repayment plans, including a standard 10-year plan or an income-based repayment plan, or negotiate an alternative repayment plan with their loan servicer.

Adapted from the glossary available at https://studentaid.gov/sa/glossary.

Before beginning repayment, students who have borrowed a Subsidized, Unsubsidized, or PLUS Loan receive exit loan counseling when they graduate, leave school, or drop below half-time enrollment. Exit counseling provides borrowers with pertinent information necessary to make informed decisions regarding both their options and the selection of their repayment plan. When borrowers enter repayment, they are assigned to one of eight federal student loan servicers that ED contracts with to facilitate the payment and collection of federal student loans. Servicers are compensated monthly based on the loan status of individuals in their portfolio. A borrower's loan servicing assignment can affect the consistency of their repayment options, the repayment plans they choose, and the outreach efforts they receive.

Federal Direct Loan Repayment

Borrowers work with their assigned federal student loan servicers to repay their student loan and any associated interest charges. There are eight plans available to borrowers for repayment of their federal student loans. Borrowers can change their repayment plan at any time to accommodate their current financial situation.

Repayment Plan Definitions

Borrowers can work with their servicer to select one of the following repayment plans. Figure 1 details the loan balance and number of borrowers in each plan.

Standard Repayment Plan: This is the federal government's default repayment plan. Under the standard repayment plan, a Direct Loan is paid off in equal monthly payments of at least $50 per month over 10 years. All borrowers and all types of Direct Loans are eligible for this repayment plan. Typically, borrowers pay less in this repayment plan over time, though the monthly payment is often higher than in other plans. For Consolidation Loans, the standard repayment period varies between 10 and 30 years, depending on the total amount of Direct Loans taken out and on other student loan debt. This repayment plan is typically used by borrowers who want to minimize the accrued interest on their student loans and who have a high enough income to make the larger monthly payments, or by borrowers who are defaulted into this plan because they have not made another selection.

Graduated Repayment Plan: Borrowers may select the graduated repayment plan for their Direct Loans. Under this plan, monthly payments are lower at first, and then are increased every two years until the loans are fully repaid after 10 years (or 10 to 30 years for Consolidation Loan holders, depending on the amount borrowed). The amount of the monthly payment varies. The minimum monthly amount will never be less than the amount of accrued interest between payments, and it will not be more than three times the payment on any other repayment plan. All borrowers and all types of Direct Loans are eligible for this repayment plan. Generally, borrowers pay more over time in this plan than in the standard repayment plan. This plan is designed for borrowers who start with low income but can reasonably expect their income to increase steadily over time.

Extended Repayment Plan: Borrowers who seek a lower monthly payment than under the standard repayment plan can select the extended repayment plan. Under this plan, the Direct Loan is paid off in equal monthly installments over a period of up to 25 years (depending on the amount borrowed). Borrowers also have the option of selecting a graduated payment amount. Under the extended repayment plan, borrowers will pay more over time than under the standard repayment plan but less per month. All borrowers and all types of Direct Loan are eligible for this plan, with a few restrictions.[6] Borrowers must have over $30,000 in either Direct Loans or FFEL loans. For example, a borrower with $40,000 in Direct Loans and $5,000 in FFEL loans can only select this repayment plan for their Direct Loans—amounts do not combine across loan programs. While this repayment plan has lower monthly payments than the standard repayment plan, borrowers tend to pay more over time due to increased accrued interest.

Pay As You Earn Repayment Plan (PAYE): PAYE is an income-driven repayment plan introduced in 2012. PAYE is available to all new Direct Loan holders (except those with Parent PLUS Loans). FFEL loan holders (except for those with FFEL loans made to parents, which are ineligible for PAYE) must consolidate their loans into a Direct Consolidation Loan to be eligible for this repayment plan. Additionally, borrowers must have received a Direct Loan on or after October 1, 2011, and had no outstanding balance on a Direct Loan or FFEL loan on or after October 1, 2007. Monthly payments are capped at no more than 10% of the borrower's monthly discretionary income based on their annual income and family size. Monthly payments must be lower than under the standard repayment plan for borrowers to be eligible for PAYE. Generally, PAYE is utilized by borrowers with a loan debt greater than their discretionary income. Borrowers must apply to ED to use this plan. Once on a PAYE plan, borrowers must recertify their income and family size each year. Because of this, monthly payments may fluctuate on an annual basis. If income reaches a point where monthly discretionary income is more than the monthly payment on the standard repayment plan, the borrower will remain on the PAYE plan, but the monthly payments will be based on the standard repayment rate, not on income (i.e., payments will never exceed what they would have been on the standard plan). Borrowers who do not annually recertify their income will be moved to a standard repayment plan and the accrued interest on their loan will capitalize. Outstanding loan balances on the PAYE plan are forgiven after 20 years of repayment, regardless of whether the borrower took on loans to fund their undergraduate, graduate, or professional education. Loan balances forgiven under the PAYE plan are considered taxable income. Borrowers who seek an income-driven repayment plan with monthly payments lower than the standard plan benefit from PAYE, though this plan is more expensive over time because of the accrued interest over a longer repayment term than the standard repayment plan.

[6] Direct Loan borrowers and FFEL borrowers must have had no outstanding balances on a Direct Loan, either as of October 7, 1998, or on the date they obtained a Direct Loan if after October 7, 1998.

Revised Pay As You Earn Repayment Plan (REPAYE): Available as of December 2015, REPAYE is an income-driven repayment plan available to borrowers with all Direct Loans except Parent PLUS Loans. FFEL loan holders (except for those with FFEL loans made to parents, who are ineligible for REPAYE) must consolidate their loans into a Direct Consolidation Loan to be eligible for this repayment plan. Borrowers must apply to ED to use REPAYE. Monthly payments are capped at 10% of a borrower's monthly discretionary income based on their annual income and family size. Borrowers must recertify their income and family size each year. Because of this, monthly payments may fluctuate on an annual basis. For borrowers with loans strictly for undergraduate education, outstanding balances will be forgiven after 20 years of repayment; for borrowers with loans for graduate or professional study, outstanding balances will be forgiven after 25 years of repayment. Forgiven loan balances under REPAYE are considered taxable income. The plan also forgives interest accrual of up to 50% on all loans and 100% of accrued interest on Subsidized Loans for the first three years. Generally, borrowers enrolled in REPAYE will pay more than the standard repayment plan over time. In addition, monthly payments may be higher than payments on a standard 10-year repayment plan, depending on the borrower's income. This plan is ideal for a borrower who seeks an income-driven repayment plan but wants to pay off their loans faster than under PAYE, or who does not qualify for PAYE based on when they borrowed their loans. Individuals who do not recertify their income or family size annually are moved to an alternative repayment plan that will pay the loan in full within 10 years from when the borrower began paying off the loan or the ending date of the 20-year (or 25-year) REPAYE repayment period, whichever is first, and interest will capitalize.

Income-Based Repayment Plan (IBR): As the name implies, IBR is a repayment plan based on a borrower's income. All Direct Loans made to students are eligible for IBR. Under IBR, monthly payments are 10% of discretionary income for borrowers who first received loans after July 1, 2014. Remaining loan balances are forgiven after 20 years of repayment. For borrowers who took out their loans prior to July 1, 2014, monthly payments are 15% of discretionary income and remaining loan balances are forgiven after 25 years of repayment. In either scenario, monthly payments do not exceed what monthly payments would have been under the standard repayment plan. Similar to the PAYE and REPAYE plans, borrowers must recertify their annual income and family size on an annual basis. As a result, monthly payments may fluctuate year to year. If income reaches a point where the monthly payment is more than the monthly payment on the standard repayment plan, the borrower will remain on the IBR plan, but monthly payments will be based on the standard repayment rate rather than income. If a borrower fails to recertify their income and family size annually, their repayment plan automatically changes to the standard repayment plan and accrued interest capitalizes. Forgiven loan balances under IBR are considered taxable income. IBR is beneficial to borrowers who have high debt relative to their income.

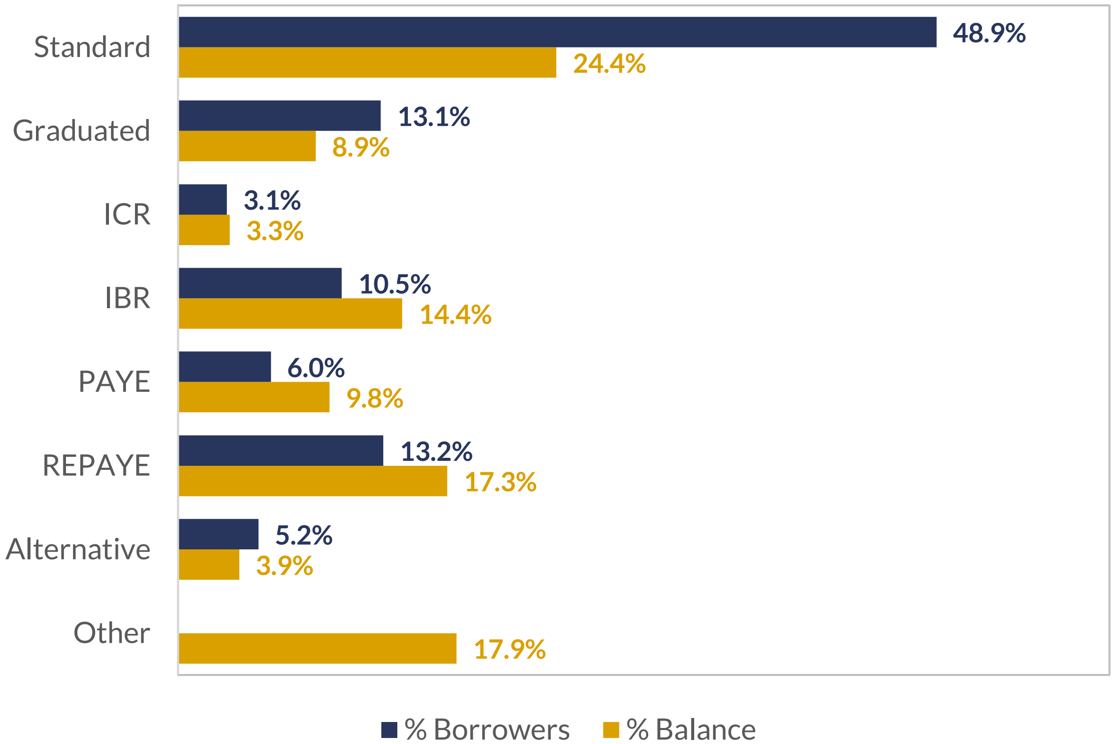
Income-Contingent Repayment Plan (ICR): Available to Direct Loan borrowers since 1994, ICR is the only income-driven repayment plan available to Parent PLUS Loan borrowers (after they fold their loans into a Direct Consolidation Loan). Under ICR, monthly payments are the lesser of either 20% of discretionary income or the monthly rate on a standard repayment plan with a 12-year term, adjusted based on income. Borrowers make payments on their loans for 25 years with ICR, and any remaining balance is forgiven after 25 years. Borrowers may be required to pay income tax on any forgiven loan balances. Borrowers must recertify their income and family size each year. Because of this, monthly payments may fluctuate on an annual basis. Unlike PAYE and IBR, monthly payments under ICR can exceed the monthly payment on a standard repayment plan. For that reason, borrowers may pay more over time on ICR than under a standard repayment plan. If borrowers do not recertify their income or family size annually, they are automatically moved to a 10-year standard repayment plan based on the amount owed at the beginning of their repayment period. As the only income-driven repayment plan for Parent PLUS borrowers, ICR is an ideal repayment plan for low-income parent borrowers seeking an income-driven repayment plan.

Income-Sensitive Repayment Plan (ISR): ISR is a temporary repayment plan only available to FFEL borrowers, including FFEL PLUS and FFEL Consolidation Loans; Direct Loan holders are ineligible for this repayment plan. FFEL borrowers who need relief on their loans may apply for ISR in which monthly payments are temporarily reduced for 12 months. FFEL borrowers work with their lender to determine an amount of their discretionary income—generally between 4% and 25%—that is greater than the monthly accrued interest on their loans. These payments are made for one year, and then the borrower must reapply for another year of ISR if needed. FFEL borrowers may only use ISR for five years. Once a borrower is off ISR, they are returned to a standard ten-year repayment plan. ISR does not extend the repayment period, so while monthly payments may temporarily be lowered, eventually, monthly payments will grow to cover the full principal. Borrowers who use ISR will typically pay more than borrowers strictly on a standard repayment plan due to increased accrued interest after a period of smaller monthly payments. Borrowers with FFEL loans facing temporary financial hardship may benefit from ISR.

While many observers use "income-based repayment" and "income-driven repayment" interchangeably, there is a key distinction between the two. "Income-based repayment" is one of the plans under the "income-driven repayment" umbrella. "Income-driven repayment" is the umbrella term used to refer to any of the five repayment plans (IBR, ICR, ISR, PAYE, REPAYE) that use a borrower's income to determine monthly payments.

Alternative Repayment Plans: All loan servicers are required to offer alternative repayment plans to borrowers if they can demonstrate that none of the existing repayment plans can accommodate their financial situation, although borrowers cannot initially select this repayment plan. These plans are only offered in exceptional circumstances, and there is no set definition of what constitutes an exceptional circumstance. Parent PLUS borrowers often enter alternative repayment plans. Borrowers with high levels of medical or private student loan debt, which are not factored into income-driven repayment plan monthly payments, may utilize alternative repayment plans. Servicers may also place borrowers who successfully rehabilitated their loan into an alternative repayment plan as they determine the most appropriate income-driven repayment plan for the borrower. These plans are or tend to be very individualized to the borrower and their circumstances.

Figure 1: Balance and Number of Direct Loan Borrowers by Repayment Plan, 2022 Q4



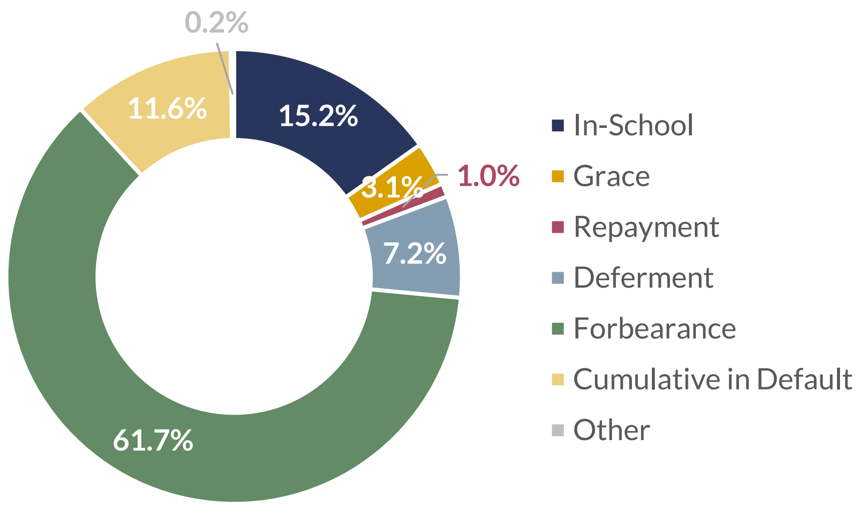
Source: Federal Student Aid, Federal Student Loan Portfolio (2022).

Repayment Status of Borrowers

Borrowers are not required to make monthly payments on their student loans when they are enrolled at least half-time at their institution. A borrower does not wait until the completion of their credential to begin repaying their loan. Certain borrowers who drop below half-time enrollment or leave their institution, whether they have completed a credential or not, are placed into a grace period before beginning repayment. The standard grace period allows borrowers to gain some financial stability and work with their loan servicer to select the best repayment plan for their situation. The standard grace period lasts six months. Parent PLUS borrowers are not eligible to receive a grace period before beginning repayment.[7] Following the grace period, borrowers go into repayment status and are required to make monthly payments on their student loans. Figure 2 highlights the repayment status of all Direct Loan borrowers.

[7] Grad PLUS Loans are eligible to receive a grace period before beginning repayment.

Figure 2: Direct Loan Borrowers by Loan Status, 2022 Q4



Source: Federal Student Aid, [Federal Student Loan Portfolio (2022)].

Variations in Repayment

While the federal government keeps records on borrowers who default, an important metric but often at the extreme end of the life of a student loan, viewing paid-in-full (PIF) rates, deferment or forbearance rates, and the ratio of the loan amount still owed can also illustrate variations in repayment. Using a 12-year follow-up to the Beginning Postsecondary Students (BPS) study by the National Center for Educational Statistics (NCES), Table 3 documents various repayment metrics in 2015 for students who entered postsecondary education in the 2003–04 academic year.

Table 3: Federal Student Loan Repayment Statuses After 12 Years of Entering Postsecondary Education, by Borrower Demographics

	Loans paid in full	Defaulted at least once	Entered deferment or forbearance at least once	Share of debt still owed
Total	**24.9%**	**27.6%**	**68.8%**	**69.4%**
Dependency status in 2003–04				
Dependent	26.1%	22.2%	66.6%	65.1%
Independent	21.4%	43.5%	75.3%	82.1%
Age in 2003–04				
23 or younger	25.3%	24.6%	68.1%	67.2%
24 or older	22.8%	42.6%	72.2%	80.6%
Pell status				
No Pell	34.6%	11.3%	58.0%	51.4%
Pell	20.3%	35.3%	73.9%	77.9%
Race/ethnicity				
White	28.4%	20.4%	64.5%	62.1%
Black or African American	10.8%	48.6%	84.4%	99.5%
Hispanic or Latino	26.0%	34.9%	70.6%	68.6%
Asian	35.7%	10.9%	53.4%	48.6%
Other or more than one race	20.1%	34.2%	74.3%	72.9%
Completion as of 2008–09				
Bachelor's	26.8%	7.9%	63.8%	60.2%
Associate	19.0%	21.3%	72.9%	77.9%
Certificate	34.1%	46.1%	69.7%	64.9%
No degree, still enrolled	15.3%	29.4%	77.6%	84.3%
No degree, left without return	27.0%	45.3%	68.1%	70.6%
NCES Table ID:	*mfdind*	*tyvzgu*	*znuwws*	*rlglix*

Source: NCES BPS:04/09, Table IDs included under each metric.
Notes: Paid-in-full rates do not include discharged student loans. Share of debt percentages are averaged. American Indian/Alaska Native and Native Hawaiian/Pacific Islander racial/ethnic groups are included in the "Other" category due to small sample sizes and unstable estimates.

Twelve years after entering postsecondary education, 24.9% of borrowers had completely paid their federal student loans off, including the principal and accrued interest. Conversely, nearly 28% had defaulted at some point and almost 70% had deferred or entered forbearance on a federal loan. On average, borrowers owed roughly 69% of their total amount borrowed. Students who were independent when first entering postsecondary education were much more likely to default or defer a loan, and typically owed 17 percentage points more relative to their amount borrowed than dependent students. Students who never received a Pell Grant were 14 percentage points more likely to have paid their loans in full after 12 years than Pell Grant recipients.

There is considerable variation by race/ethnicity, where nearly 36% of Asian students and 28% of white students had PIF, compared to only 10.8% of Black students. Black students also owed the most relative to their amount borrowed after 12 years; on average, they owed nearly the same amount that they borrowed. In contrast, Asian students owed less than half of what they borrowed after 12 years, white students owed 62%, and Hispanic or Latino students owed 68.6%.

Certificate recipients had the highest PIF rate, with 34% of borrowers having fully paid off their loans after 12 years.[8] Understandably, students that were still enrolled had the lowest PIF rates, given that they may not have yet entered repayment. The data for associate degree recipients tell an interesting repayment story; though they have low PIF rates, they also are the second least likely to have defaulted on a federal loan. They owe the second highest amount relative to their amount borrowed, however, suggesting that they are slowly but consistently managing their payments. Bachelor's degree recipients, on the other hand, almost never default on their loans and owe the least amount relative to their amount borrowed. The data on those students who left school without returning are a concern; they are the second most likely to default and typically owe 71% of their amount borrowed without having received a credential.

Table 4 displays the repayment statuses of borrowers by institutional sector. Though PIF rates vary little by sector, borrowers at private for-profit institutions are much more likely to default on their loans after 12 years; more than half have defaulted at some point in that time period. For-profit borrowers are also the most likely to defer payments and typically owe the most relative to their amount borrowed out of any institutional sector. Borrowers at public four-year and private non-profit institutions have nearly identical repayment profiles, with the slight exception of higher deferment or forbearance rates at private non-profits.

[8] This is likely due to the fact that certificate completers borrow the least amount of federal loans. See BPS:04/09, Table ID: xexegp.

Table 4: Federal Student Loan Repayment Statuses After 12 Years of Entering Postsecondary Education, by Institutional Sector

	Loans paid in full	Defaulted at least once	Entered deferment or forbearance at least once	Share of debt still owed
Institutional Sector				
Public four-year	25.5%	17.6%	65.9%	64.2%
Public two-year or less	22.9%	26.2%	67.2%	74.0%
Private non-profit	25.3%	18.4%	70.2%	63.9%
Private for-profit	27.0%	53.5%	74.8%	74.5%
NCES Table ID:	*mfdind*	*tyvzgu*	*znuwws*	*rlglix*

Source: NCES BPS:04/09, Table IDs included under each metric.
Notes: Paid-in-full rates do not include discharged student loans. Share of debt percentages are averaged.

All Direct Loan borrowers having difficulty with repayment are eligible for certain protections, such as deferment and forbearance.[9] Borrowers facing financial hardships in which they are willing to make payments on their loans but unable to make their full payments are eligible for forbearance. When a loan is in forbearance, a borrower is only able to make payments on interest; principal payments are prohibited. Borrowers switching between a standard plan and an income-driven repayment plan are placed on administrative forbearance during the switch between repayment plans, which may take several weeks to complete.[10]

[9] The timeline for deferment varies depending on type but typically does not last longer than three years. General forbearances last no longer than 12 months, though you may request multiple general forbearances with a cumulative maximum duration of three years. Mandatory forbearances imposed on your lender depend on the circumstances.

[10] In response to the COVID-19 pandemic, Congress and the Department of Education placed Direct Loan borrowers and defaulted FFEL accounts into administrative forbearance, the COVID-19 forbearance. Accounts in this forbearance are not accruing interest, and borrowers can defer payments through June 30, 2023. The forbearance counts toward Public Service Loan Forgiveness, as well as income-driven repayment forgiveness for qualified borrowers, two programs to be discussed later in this primer. Additionally, collections on defaulted accounts have stopped during this time frame.

Federal Loan Forgiveness

Public Service Loan Forgiveness

Individuals employed by government entities or not-for-profit organizations may be able to receive loan forgiveness under the Public Service Loan Forgiveness (PSLF) Program. Under PSLF, a borrower's remaining balance on Direct Loans is forgiven after 120 qualifying monthly payments while working for a qualified employer. The qualifying monthly payments do not need to be consecutive. In order to qualify for PSLF, a borrower must meet four basic conditions:

1. The borrower must work full-time for an approved government entity or not-for-profit organization.[11]
2. The borrower must have Direct Loans.
3. The borrower must be enrolled in an income-driven repayment plan (if a borrower remains on a 10-year standard repayment plan for the duration, there would be no loan balance to forgive, though they could be enrolled in standard repayment for some of the 10-year period).
4. The borrower must make 120 qualifying monthly payments under these conditions.

Qualifying payments cannot be made when the borrower is in school, in their grace period, or in deferment or forbearance, with the exception of the COVID-19 administrative forbearance. Either throughout the PSLF process or at least prior to submitting the 120 payments for forgiveness, the borrower must certify each of their employers that qualify under PSLF rules. While it is possible to submit all certification documentation just prior to forgiveness, borrowers are encouraged to recertify their employer regularly to verify that payments count toward PSLF. If they wait, they would need to submit forms from employers they no longer work for. Borrowers must also annually recertify their income to remain on an income-driven repayment plan. In the fall of 2020, ED combined two forms—the employer certification form and application for forgiveness— meaning borrowers will no longer have to submit a separate application.[12] With the change to one form, ED will now be able to automatically process forgiveness. Forgiven loan balances under PSLF are not considered taxable income by the IRS.

In 2020, ED unveiled the PSLF Help Tool 2.0 to help borrowers determine which documents they must submit to enroll and whether their employer qualifies them for PSLF. While borrowers are still required to physically print the resulting document for their employer to sign, both employee and employer will eventually be able to sign the verification document electronically through the Help Tool. This tool also allows borrowers to keep track of how many qualifying payments they have made toward loan forgiveness. The counter updates each time the borrower submits an employment certification form that can be confirmed.

[11] Government organizations at any level (federal, state, local, or tribal), non-profit 501(c) organizations, other non-profit organizations who provide certain public services, and full-time AmeriCorps or Peace Corps volunteers are eligible for PSLF. For more information on qualifying employment, visit the Public Service Loan Forgiveness page on ED's website.

[12] Once a borrower's employer certification form is submitted and approved as a qualifying employer toward loan forgiveness through PSLF, the borrower's loans are transferred to MOHELA, the federal government's contracted loan servicer for all PSLF-eligible loans as of July 2022.

PSLF Application Issues:

When the first borrowers eligible for PSLF were able to begin submitting applications in September 2017 for loan forgiveness, over 99% of applications were rejected. Data shared by ED in 2019 demonstrated that over 80% of the applicants who were denied were rejected because they had not held a loan for at least 10 years, the minimum period to qualify for PSLF. Other applications were rejected because the borrower did not meet basic program requirements, such as having Direct Loans, working for a qualified employer, or having made 120 qualifying payments. Borrowers also noted instances where their loan servicer provided incorrect information regarding PSLF eligibility or delayed transferring loans into qualifying repayment plans or to the Pennsylvania Higher Education Assistance Agency (PHEAA), the PSLF servicer at the time. In 2018, the GAO also found that ED was not doing enough outreach to PSLF borrowers as required by law.

In 2018, Congress passed the Consolidated Appropriations Act, which temporarily expanded the conditions under which borrowers may be eligible for loan forgiveness under PSLF. The loan forgiveness program created under this law is referred to as Temporary Expanded Public Service Loan Forgiveness (TEPSLF). TEPSLF allows borrowers whose PSLF applications were denied only because some or all of their monthly payments were not made under a qualifying repayment plan to receive loan forgiveness, as long as the payments they did make were under certain other plans (Graduated, Extended, or Consolidation) and, 12 months prior to applying, were at least as much as they would have been under a qualifying repayment plan. Borrowers whose PSLF applications were rejected for a reason other than their repayment plan are not eligible for TEPSLF. Loan balances forgiven under TEPSLF are not considered taxable income by the IRS. To apply for TEPSLF, borrowers must submit a forgiveness form through the Help Tool.

To track PSLF applications and program data, ED releases quarterly reports on the PSLF program. Despite greater awareness of the PSLF program and the introduction of TEPSLF, 98% of PSLF applicants through September 2020 were still being rejected and only 8,400 borrowers received loan discharges under the program through April 2021.[13] Following the introduction of the combined application/certification form in fall 2020, between November 9, 2020, and June 30, 2021, 497,000 borrowers submitted an employer certification form; 225,000 of these forms were processed, 97,000 were rejected as incomplete, and 175,000 forms remain to be processed.

In October 2021, ED announced a temporary waiver of certain PSLF requirements until October 2022. The changes allow any previous payment made during qualifying employment to count toward PSLF forgiveness regardless of loan program, repayment plan, or whether the payment was made on time. FFEL or Perkins Loan borrowers who previously did not qualify for PSLF could consolidate their loans into the Direct Loan program prior to October 31, 2022, to gain credit for past periods of repayment. The waiver discharges made a significant difference in the rate of PSLF forgiveness. As of October 2022, 233,320 borrowers had received $14.9 billion in PSLF discharges—92% of which occurred under the waiver.[14] The number of borrowers who receive loan forgiveness under PSLF is expected to grow in the coming years.

[13] See the Federal Student Aid (2022) data on PSLF.

[14] See Federal Student Aid (2022), Public Service Loan Forgiveness Data.

Teacher Loan Forgiveness Program

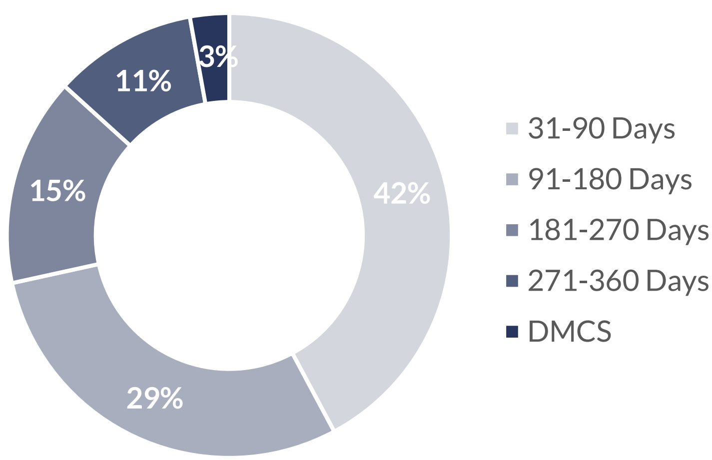
Another federal loan forgiveness program for borrowers is the Teacher Loan Forgiveness Program. Teachers who work in a low-income school or other education service agency for five consecutive years, among other conditions, are eligible to receive up to $17,500 in loan forgiveness on their Direct Loans or FFEL loans. PLUS and Perkins Loan holders are ineligible for this program. The actual loan forgiveness amount is based on the subject taught. Eligible teachers may qualify for both the Teacher Loan Forgiveness Program and PSLF, although payments made under one program do not count toward the other. Therefore, a qualifying teacher would need to make qualifying payments for five years under the Teacher Loan Forgiveness Program and then 120 payments under PSLF. Once the required payments have been made, eligible teachers must submit an application to their loan servicer for teacher loan forgiveness.

Federal Direct Loan Delinquency and Default

Federal Loan Delinquency

When borrowers do not make on-time payments according to the terms of their promissory note, their loan is considered delinquent. The student loan will remain delinquent until the missed payment is made, or until the borrower enters deferment or forbearance. Once a loan becomes 60 days delinquent, federal law requires lenders to report the delinquency to credit monitoring agencies. See Figure 3 for a breakdown of 2020 delinquency status prior to the implementation of the COVID-19 administrative forbearance.

Figure 3: Direct Loan Portfolio by Delinquency Status, 2020 Q2



Source: Federal Student Aid, Federal Student Loan Portfolio (2022).
Pre-pandemic data is provided to illustrate typical delinquency status patterns.

A borrower can be delinquent without defaulting on their loan. When a loan is delinquent for less than 270 days, the delinquent account may be reported to a crediting agency, much in the same way that a late credit card payment is reported. Borrowers with delinquent accounts remain eligible to receive additional federal student loans. Once accounts are paid, the borrower returns to active repayment status. It is only once an account is 270 or more days delinquent that borrowers begin facing further repercussions.

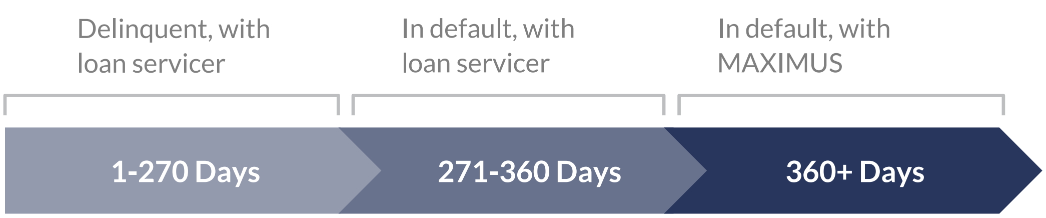
Federal Loan Default

If a borrower fails to repay their loan outside of deferment or forbearance for 270 days, the borrower defaults on their loan. When a borrower defaults on Direct Loans, the federal government has the ability to garnish the borrower's wages, withhold or reduce Social Security benefits, or deem the borrower ineligible for further student aid. Direct Loans, like private education loans and FFEL loans, are not generally dischargeable through bankruptcy. The guarantor of the loan, the institution that granted the loan, and the federal government have additional tools at their disposal to recover the owed funds, beyond the aforementioned government powers. These entities may report the default to consumer reporting agencies or file a civil lawsuit. To exit default, borrowers can either repay their loans in full or consolidate or rehabilitate their loans through their loan servicer. Notably, using 2012 data, the Department of the Treasury found that 70% of defaulted borrowers would have been eligible for lower monthly payments under an income-driven repayment plan.

Institutions have a keen interest in the default rates of their students. Institutions whose cohort default rate exceeds a certain threshold lose access to federal student aid. The cohort default rate is the percentage of students attending an institution who default on their student loans within three years of beginning repayment.

For the first 90 days after a borrower defaults, the loan servicer retains the loan and attempts to collect on it. If they are unable to do so, the loan servicer transfers the defaulted loan to ED, and ED attempts to collect on the loan. In November 2021, ED announced that it would no longer be transferring ED-held defaulted loans to private collection agencies (PCA). Prior to this new rule, at 425 days delinquent, ED would transfer the defaulted loan to one of 11 PCAs to recover the defaulted loans. Currently, loans that are in default for more than 360 days are transferred to MAXIMUS Federal Services, Inc., a private loan servicer contracted by ED. Figure 4 shows the entire timeline of a loan entering delinquency and default.

Figure 4: Timeline of Delinquency and Default



Source: Federal Student Aid.

A defaulted account reported to a credit monitoring agency remains on a borrower's credit report for up to seven years. A defaulted loan is removed from the borrower's credit report if the loan is successfully rehabilitated. Defaulting on student loans harms a borrower's credit score and can adversely affect their ability to secure a private loan (e.g., a car loan or a mortgage). Many borrowers who default eventually return their loan to good standing, but the repercussions remain.[15]

Variations in Default

While data on student debt exists, and repayment rate data at the institution level is published in the College Scorecard, there is a dearth of data on individual borrowers in repayment. ED publishes cohort-based data on the types of borrowers who take on loans to fund their education, the balance of those loans, and the sector of institution they attend, but there is little federal demographic information on borrowers in repayment and the repayment plans they choose. However, there is some existing demographic data on default. ED also publishes cohort-based longitudinal survey data on student loan default and delinquency. The data that does exist paints an incomplete portrait of student loan repayment.

The median defaulter takes out only $9,600, just over half of what the median non-defaulter takes out.

The BPS:04/09 data by the Center for American Progress (CAP) documents student loan default by several demographic variables. Among students who began postsecondary education in 2003–04, 25% of borrowers had an expected family contribution of $0, yet these borrowers accounted for 43% of all defaulters. Forty percent of all defaulters came from families in the lowest quartile of family income. Eighty-seven percent of defaulters from this cohort received a Pell Grant. For students at the higher end of the income spectrum, only 10% of defaulters came from families in the top income quartile (who account for one-fifth of all borrowers). Dependency status was also associated with default; independent students with dependents were the most indebted. These students, 17% of all borrowers, account for 29% of all defaults.

The association between race and student loan default and repayment is well documented. White students accounted for 60% of all borrowers from the cohort of students who enrolled in 2003–04 but only 44% of all defaulters. Despite accounting for only 17% of all borrowers, Black borrowers accounted for 30% of all defaulters. Hispanic borrowers were 14% of all borrowers from this cohort but were 18% of all defaulters. Generally, data show that Black borrowers and low-income borrowers borrow more than white peers to receive identical degrees. Borrowers of color are more likely to drop out than white borrowers, which further exacerbates default rate disparities by race. Nearly 50% of Black borrowers who first entered college in 2003–04 and took out federal loans defaulted within 12 years of entry. Sixty-five percent of Black borrowers who dropped out defaulted, compared to 46% of dropouts overall. Of the cohort, 29% of all students defaulted. Even among completers there are racial disparities. Six percent of white borrowers with a bachelor's degree defaulted within 12 years of entry, while 23% of Black borrowers and 14% of Hispanic borrowers with bachelor's degrees defaulted.

[15] For instance, 28.7% of borrowers had their most recent defaulted loan paid in full or discharged, while 26% took steps such as consolidation or rehabilitation to remedy their defaulted loans. See BPS:04/09 Table ID: uogjqt.

In many cases, borrowers left school without completing a credential, leaving with debt and little to no means to a higher income (e.g., a credential or a degree). CAP found that 46% of defaulters dropped out before completing a credential and the median loan balance at time of default for these non-completers was $9,336. Students who drop out before completing a credential are 30% of all borrowers. Borrowers who completed their credential typically have higher loan balances, despite being less likely to default on their loans than their peers who drop out. Given that their credential ostensibly contributed to a greater chance of employment or higher wages, loan payment is typically more manageable.

Borrowers who attend private for-profit institutions are most likely to default. While only 19% of borrowers first attend a for-profit institution, 38% of all defaulters attended a for-profit institution. Borrowers who attend a private non-profit four-year institution are least likely to default. These borrowers make up 17% of all borrowers, but only 11% of defaulters. These characteristics of defaulters are not isolated. In fact, many intersect and compound to exacerbate problems with repayment and overall debt. Completion status, institutional sector, and racial intersections show striking disparities. Seventy-five percent of Black borrowers who dropped out of a for-profit institution default, compared with 50% of white borrowers and 63% of Hispanic borrowers. Even at four-year public institutions, results vary. Sixty-four percent of Black dropouts default and 50% of Hispanic dropouts default, compared to 39% of white dropouts.

COVID-19 Pause and Resumption of Payment

As mentioned above, Congress and ED placed Direct Loan borrowers and defaulted FFEL accounts into administrative forbearance in response to the COVID-19 pandemic. In this COVID-19 forbearance, accounts are not accruing interest, and borrowers can defer payments through June 30, 2023. Additionally, the forbearance counts toward PSLF and for forgiveness under income-driven repayment plans. Furthermore, ED has ordered collections on defaulted accounts to cease.

Restarting the repayment system will be a massive undertaking. ED data shows that only 400,000 Direct Loan borrowers were in active repayment as of December 31, 2022; the remaining 34.6 million Direct Loan borrowers and 1.1 million defaulted FFEL borrowers are scheduled to begin repayment after June 30, 2023. Several servicers laid off call center employees during the pandemic due to a decrease in contacts from borrowers, as well as lower revenues primarily caused by a lower negotiated fee for accounts in the COVID-19 forbearance—which now account for the majority of servicer portfolios. These servicers will need to rehire employees and train new staff in time for the anticipated deluge of questions from borrowers upon the restart of repayment.

Recent surveys have shown that borrowers are concerned about their ability to make full, on-time payments once repayment starts.[16] A June 2021 Pew Charitable Trusts survey found that two-thirds of borrowers would have had difficulty making student loan payments in July. Eighty-five percent of these borrowers said they would have difficulty making payments in six months, and 69% percent report they would have difficulty making payments in 12 months.[17] Advocates are concerned that high numbers of borrowers will go delinquent or default on their loans upon restarting repayment.

[16] When these surveys were conducted, the pause in repayment extended only until September 30, 2021. This explains why the surveys did not ask borrowers about their ability to begin repayments at that time.
[17] See the Pew Charitable Trusts (2021).

Next Gen: A Unified Loan Servicer Interface

Given the complexities of the student loan repayment system, ED has sought to revamp the loan servicing process. Currently, ED contracts with eight different loan servicers, most of which use their own systems and websites for interacting with borrowers; there is no uniform loan servicing experience for borrowers due to the number of different servicers and systems. In 2017, ED announced its plans for a Next Generation Financial Services Environment (Next Gen). Next Gen would create one uniform FSA-branded platform that contracted servicers use to interact with borrowers. Borrowers will still be assigned to a loan servicer, but borrowers across loan servicers will use a central platform, customer service line, and email for loan servicing-related issues. Because of this, it is possible that borrowers will not realize that ED itself is not servicing their student loan.

As currently envisioned, this central platform would connect with a mobile application that will enable current and prospective borrowers to access the FAFSA and, eventually, their repayment options. A streamlined process would eventually enable students and their families to complete the FAFSA, receive financial aid, make monthly payments, and apply for loan forgiveness through one portal.

In October 2020, ED released a new procurement for an Interim Servicing Solution (ISS) that would award two five-year servicing contracts, similar to the existing servicer contracts. The ISS would have served as a bridge until ED could complete the Next Gen procurement and debut a new platform. In December 2020, the Consolidated Appropriations Act of 2021 prohibited ED from awarding funding for any contract solicitation for Next Gen and permitted FSA to extend the contracts of existing loan servicers for up to two additional years when they expire at the end of 2021. Following ED's announcement of their intention to extend servicer contracts at the end of 2021, FedLoan Servicing (PHEAA) and Granite State announced they would no longer service federal student loans and did not extend their contracts.[18] Additionally, while Navient signed a contract extension, ED approved the transfer of Navient's federal servicing portfolio to a new company, Maximus. As a result, the ISS solicitation has been put on pause.[19]

Conclusion

Student loans help fund postsecondary opportunities for many students who would otherwise be unable to attend. This increased opportunity comes at a cost, however, as loans always come due. Federal responses to repayment difficulty range from creating income-based repayment plans to expanding loan forgiveness and discharges. Understanding how the federal government impacts repayment requires understanding the life cycle of student loans and who disproportionately struggles to repay. Variations in repayment rates, deferment, and default rates by borrower demographics and institutional sector are important considerations for policymakers who hope to identify potential consequences of the federal student loan repayment system.

[18] In July 2022, the loan servicer MOHELA took over control of the volume from PHEAA.

[19] For more information on servicing contracts, see the Federal Student Aid Data Center and ED's Fiscal Year 2022 Budget Request. For additional information on loan servicing, see PNPI's Loan Servicing Primer.

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