

Estimated Costs of the Proposed Rule on Income-Driven Repayment

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What This Presentation Will Cover

- Background on federal student loan budgeting
- Summary of the proposed rule on income-driven repayment (IDR)
- The Congressional Budget Office's cost estimate of the proposed rule
 - Analysis of outstanding loans and projections of future loans
 - Behavioral effects driven by policy changes
 - Uncertainty

Student Loans in the Federal Budget

How Is the Cost of the Federal Student Loan Program Reflected in the Federal Budget?

- The federal budget is recorded primarily on a **cash basis**: Transactions are recorded when payments are actually made or receipts are collected.
- The Federal Credit Reform Act (FCRA) requires that federal credit programs (including student loans) be recorded on an **accrual basis**: Each transaction is recorded as a single number that represents the anticipated net federal cash flows over the lifetime of the loan, discounted back to the year in which the loan originated.

How Are the Costs of Making Changes to Loans Recorded?

- Changes to **outstanding loans** are called loan modifications
 - Executive actions or legislation that change expected cash flows of existing loans also affect their net cost.
 - The entire net cost (on a net present-value basis) is recorded in the year in which the loans are modified.

- Changes to **future loans**
 - Executive actions or legislation that affect the cost of future loans are recorded in the year the new cohort of loans is originated.



Overview of the Proposed Income-Driven Repayment Plan

What Are the Major Changes in the Proposed IDR Plan?

- Increases the amount of income exempted from the calculation of monthly payments to 225 percent (from 150 percent) of the federal poverty guidelines;
- Reduces the amount of discretionary income that undergraduate borrowers pay to 5 percent (graduate borrowers continue to pay 10 percent);¹
- Eliminates the accrual of unpaid interest when a borrower's payment does not cover the entire amount of interest due;
- Allows borrowers with lower balances to receive early forgiveness; and
- Authorizes the Department of Education to automatically enroll borrowers in an IDR plan if they are 75 days delinquent on payments.

1. Borrowers with undergraduate and graduate loans would pay a percentage of their discretionary income based on the weighted average of their combined loan amounts.



Analysis and Estimate

CBO's Method

To estimate the cost of the proposed IDR plan, CBO assumed that the Administration's loan cancellation will take effect. (CBO will update its assumptions about debt cancellation when the Supreme Court announces its decision.)

CBO developed a statistical model using:

- Historical data from the National Student Loan Data System (NSLDS), and
- The agency's projections of other factors, including borrowing, educational attainment, income, and family size.

In estimating the costs, CBO also consulted with experts on postsecondary financial aid and incorporated existing literature on student aid.

Costs of the Proposed IDR Plan: Overview

Total cost: **\$230 billion**

- **\$76 billion** in outstanding loans (those that originated before 2023), recorded in fiscal year 2023.
 - If the Supreme Court fully invalidated the Administration’s loan cancellation plan, there would be roughly an additional \$45 billion in costs to outstanding loans.
- **\$154 billion** in new loans (those originated between 2023 and 2033), recorded in the year each new cohort of loans is originated.

Costs of the Proposed IDR Plan: Outstanding Loans

At the end of fiscal year 2022, there was \$1.3 trillion in outstanding direct loans to students. Roughly 50 percent of the volume of those loans in a repayment plan is owed by borrowers in an IDR plan.

In CBO's baseline, about \$900 billion remains after loan cancellation, and 57 percent of the remaining volume is in IDR plans.

Under the proposed changes, the volume of direct student loans in IDR plans increases to 66 percent for two reasons:

- Some borrowers in fixed-length repayment plans select the proposed IDR plan.²
- Delinquent borrowers are automatically enrolled if they have authorized disclosure of income and tax return information to the Department of Education.

2. The number of borrowers who would choose to move into IDR plans is based on the present value of the payment reduction that borrowers could receive under an IDR plan.

Costs of the Proposed IDR Plan: New Loans

CBO's estimate of the costs of the proposed IDR plan for new loans is based on three main factors:

- **Reduced borrower payments.** Underlying policy changes would lead to most borrowers paying less each month, and less overall, on a net present-value basis.
- **More borrowers in IDR plans** (including delinquencies being automatically moved in). CBO estimated the likelihood of borrowers moving from fixed-term plans into IDR plans on the basis of monthly payment reduction, historical data, and other factors.
- **Increased volume of loans.** If borrowing was less costly, more students would borrow and projected future borrowers would borrow more.

Increases in the Volume of Loans and Other Behavioral Considerations

Overall, annual volume of direct student loans increases by about 12 percent (or about \$10 billion) by fiscal year 2027.

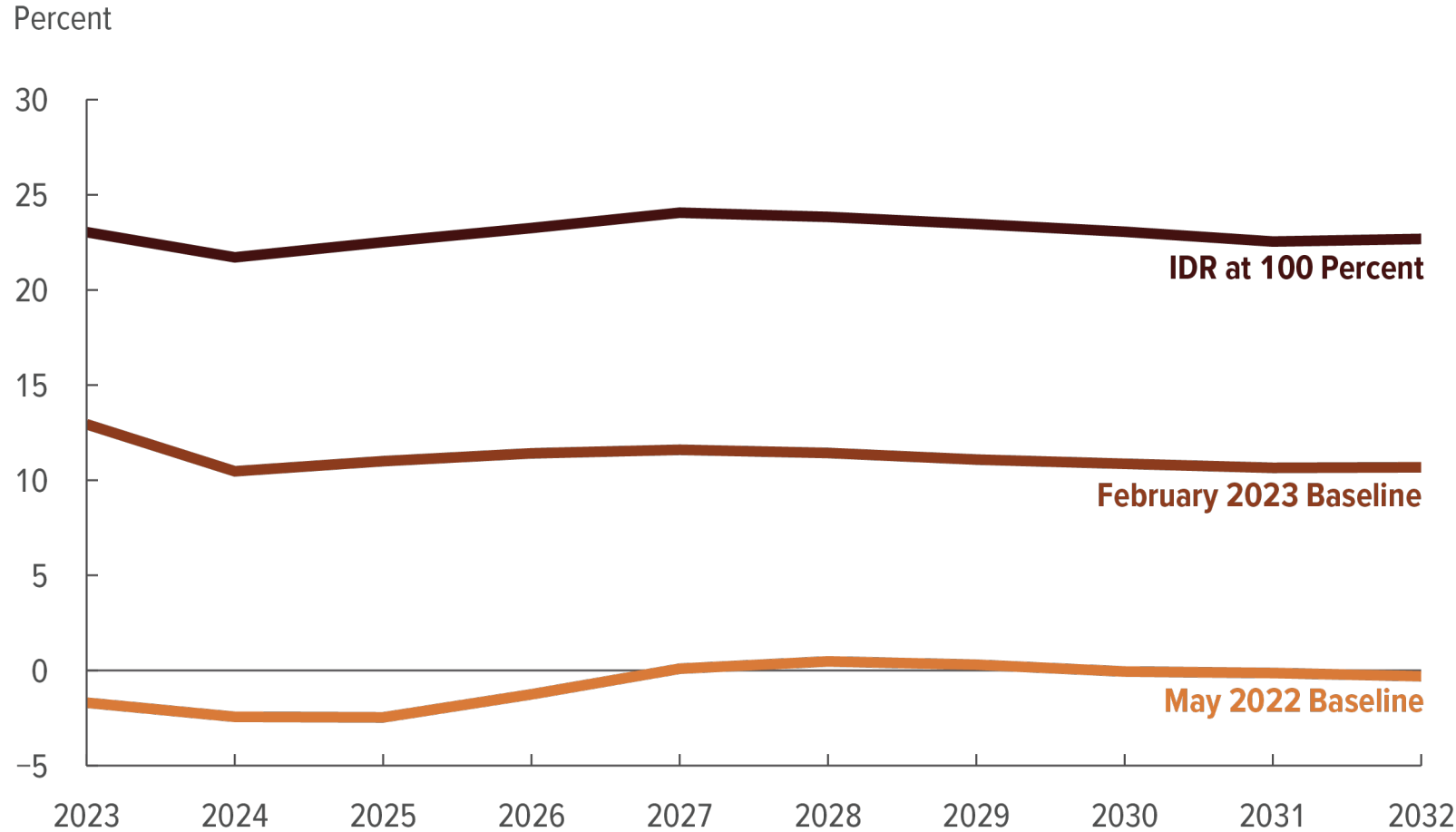
- Borrowing for undergraduate education increases by about 15 percent.
- Borrowing for graduate education increases by about 10 percent.³

Sources of increase:

- Students who would be expected to take out federal loans would borrow more.
- Some students who would not be expected to borrow under current law would take out loans.
- Responses to the proposed IDR plan by postsecondary institutions could affect borrowing.
 - Tuition increases
 - Student financial aid offices
 - Institutional accountability regulation

3. These estimates represent the middle of the distribution of potential outcomes.

Subsidy Rate Changes



The subsidy rate is the cost of a program, calculated following the procedures specified in the Federal Credit Reform Act of 1990 (P.L. 101-508), divided by the amount disbursed. The higher the projected subsidy rate, the higher the projected cost of the loans to the government.

For this figure, CBO calculated the subsidy rate using full cost of the proposed IDR rule under the February 2023 baseline rather than using 50 percent of the costs of the proposed rule.

Uncertainty

- It is difficult to anticipate how students and postsecondary institutions would respond to the proposed plan.
- How broadly the plan was publicized would affect the number of borrowers and loan volume.
- Projections of borrowers' earnings, family size, and tax-filing decisions are all inherently uncertain.



Questions?

Comparison of CBO's and the Department of Education's Estimates

CBO

- Estimated cost: \$230 billion
- Assumed behavioral changes: increased IDR take up and volume increases
- Estimate covers the 2023–2033 period

Department of Education

- Estimated cost: \$138 billion
- Assumed no behavioral effects for new loans
- Estimate covers the 2023–2032 period (if their projection window was the same as CBO's, their estimate would be higher)

CBO and the Department of Education also may differ in their projections of income, tax-filing status, interest rates, discount rates, loan volume, and baseline enrollment in IDR plans.

Relevant Links

- For the notice of proposed rulemaking (NPRM), see Improving Income-Driven Repayment for the William D. Ford Federal Direct Loan Program, 88 Fed. Reg. 1894 (January 11, 2023), <https://tinyurl.com/465r5ad3>.
- For CBO's estimate of the NPRM's effects, see Congressional Budget Office, letter to the Honorable Virginia Foxx and the Honorable William Cassidy providing an estimate for the costs of the proposed income-driven repayment plan for student loans (March 13, 2023), www.cbo.gov/publication/58983.
- For CBO's estimate of H.R. 2811's effects, see Congressional Budget Office, cost estimate for H.R. 2811, the Limit, Save, Grow Act of 2023 (April 25, 2023), www.cbo.gov/publication/59102.