The Federal Student Loan Knowledge Gap

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Exploring What Borrowers Think They Know About Their Education Debt Before Monthly Payments Resume

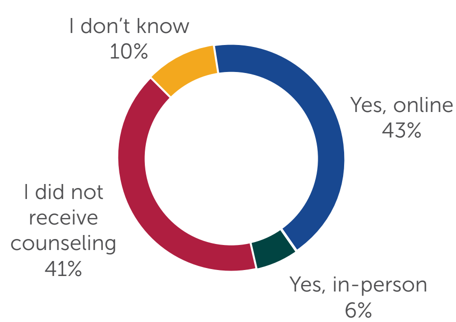
Most federal student loan borrowers have not had to make a loan payment in over 40 months due to federal COVID-19 emergency relief measures, including hundreds of thousands of borrowers who exited college during the pandemic and have not yet been required to make a student loan payment.

Student Loan Counseling and the Complicated System

Given the complexity of the higher education financing system and the gravity of the decision to borrow loans, the federal government requires that federal student loan borrowers complete loan counseling twice – before the first disbursement of the first loan (called entrance counseling) and before the student graduates, has fallen below half-time enrollment, or dropped out of college (called exit counseling). This counseling can be completed a number of different ways, but most institutions require their students to complete the Department of Education's online modules as that is the easiest way to ensure that all required topics are covered sufficiently.

The number of required topics has increased exponentially over the decades. The four original required elements ballooned to 28 topics as of 2023.[1,2] This volume of information can be difficult for students to absorb in a short amount of time. Research indicates the volume and complexity of information delivered during consumer education is important to retention of the information. Whenever information is provided in large and complex forms, consumers make poor financial choices.[3,4]

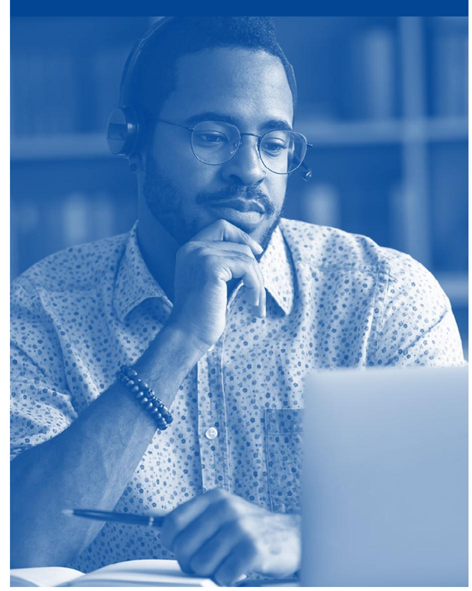
When you first received your your student loan, did you receive any in-person or online counseling that informed you about your student loans?*



**Of those who said they had borrowed a student loan*
Source: Trellis Company, Fall 2022 Student Financial Wellness Survey

Key Takeaways

- The complicated federal student loan system hinders students' ability to successfully repay their obligations.
- The tens of millions of borrowers that collectively owe over a trillion dollars of taxpayer-backed debt deserve more and better information before entering repayment this fall.
- Improved financial literacy education could enhance family decision-making processes and prevent future student loan repayment challenges.

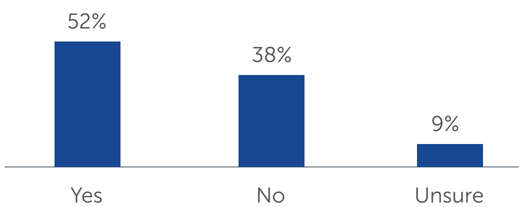


A large survey of currently enrolled students in fall 2022 found that only about half of respondents with student loans remembered receiving loan counseling when they first borrowed. Fifty-one percent of borrowers did not know if they had loan counseling or thought they did not, indicating that the counseling borrowers currently receive is not having a lasting impact for many of them.[5]

Borrower Awareness

The complexity of the system and the large number of topics covered in a loan counseling session makes it unsurprising that many borrowers are unaware of important aspects of their loans and repayment. In a 2022 survey by New America, just over half of student loan borrowers were aware of income-driven repayment (IDR) plans. More than a third (38 percent) said they had not heard of these plans and nine percent were unsure, meaning nearly half of borrowers in this survey were unaware of these beneficial plans.[6]

Have you ever heard of income-driven repayment plans before?*



**Of survey respondents who reported borrowing student loans*
Source: New America, Varying Degrees 2022

Borrowers will have a new repayment option when required payments begin later this year. The Saving on a Valuable Education (SAVE) plan will replace the REPAYE plan and provide the lowest monthly payments of any IDR plan. Borrowers will also have an extended on-ramp period once repayment begins to help transition them back into regular payments. IDR plans and the extended on-ramp period will provide an important safety net to borrowers as they navigate loan repayment in addition to their other financial obligations. Changes to the repayment options and the on-ramp period need to be conveyed to borrowers by the Department of Education.

Borrowers should contact their student loan servicer as soon as possible for assistance to prepare for repayment. However, millions of student loan borrowers will make payments to a new servicer when repayment starts up again due to changes in the federal servicing contracts. The Consumer Financial Protection Bureau (CFPB) estimates that 44 percent of student loan borrowers have had their loans transferred to a new servicer due to several large servicers exiting their contracts with the Department of Education over the last three years. The transfer process may complicate repayment for some borrowers as they may need to complete additional tasks to ensure smooth payments, such as re-enrolling in processes or updating information.[7]

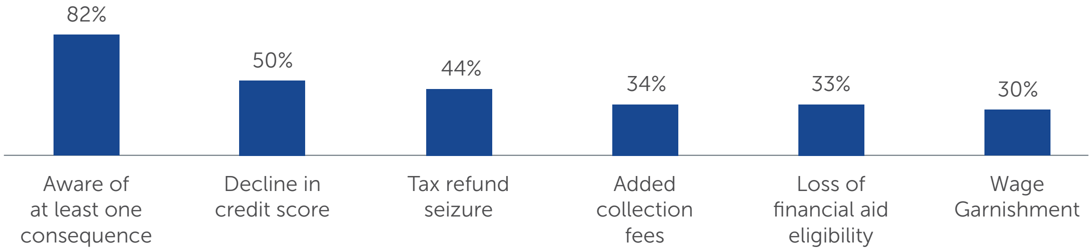
The CFPB examined borrowers who had been in active repayment prior to the COVID-19 repayment relief measures and still had a balance as of March 2023 and found that the percentage of student loan borrowers with delinquencies on credit products besides student loans is higher now than it was before the pandemic. The CFPB report highlighted the importance of this finding, saying that "student loan borrowers who are already having difficulty with their other payment obligations are especially likely to struggle with their student loan payments if they don't get some sort of payment relief like enrolling in an IDR plan."[8]

Research has shown that many borrowers prioritize other debt payments over student loans when money is tight.[9] This could be due to a lack of awareness of the myriad consequences of student loan default and the feeling of immediacy of the consequences for delinquency and default on other types of credit products. Not paying the electricity bill will result in having the electricity shut off in short order. Not paying the credit card bill adds noticeable fees to the next bill. The consequences of student loan default are no less severe but take longer to manifest.

According to a 2021 survey by Pew Charitable Trusts, among student loan borrowers who had experienced default, 82 percent were aware of at least one consequence prior to defaulting. However, awareness of each specific consequence varied. Half of these borrowers reported being aware of potential declines in their credit score and 44 percent said they knew their tax refund could be seized. Only about a third of respondents were aware of collection fees and the loss of financial aid eligibility, and only 30 percent were aware their wages could be garnished.[10]

Many borrowers expressed regret over their borrowing decisions in a 2015 survey. Over half (53 percent) said they would make a change if they could go through the process of taking out loans all over again. Only 29 percent said they would take the same actions, and 17 percent were unsure.[11] Less than a third of currently enrolled borrowers in a fall 2022 survey said they were confident or very confident they will be able to pay off the debt they acquire as a student.[12]

Prior awareness of consequences of default among defaulted student loan borrowers



Source: Pew Charitable Trusts, 2021 student borrowers survey

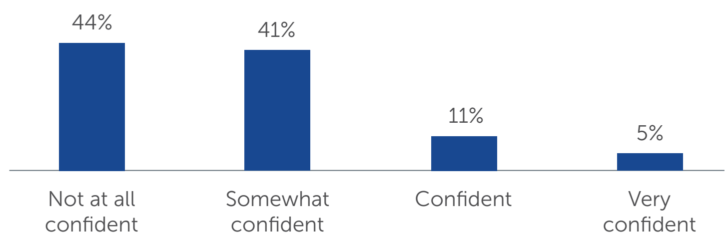
Repayment Concerns

As of 2023, more than 38 million borrowers owed $1.4 trillion in federal direct student loans. These borrowers are about to begin repayment after a break of several years, or for the first time for those who would have entered repayment for the first time during the pandemic, and many will struggle to afford the payments. In a 2022 survey by New America, just over half of student loan borrowers said it was somewhat difficult or very difficult to afford their student loan payments before the pandemic. About the same percentage of borrowers said it would be somewhat difficult or very difficult to afford their student loan payments if they had to resume loan payments in 12 months.[13]

Complicating matters further, borrowers are unclear on whether they might receive some form of student loan forgiveness. More than half had some level of confidence they would have some or all of their loans forgiven in the future, while a little less than half were not at all confident this would happen.[14] This lack of clarity adds to the confusion that borrowers have regarding their obligations and what forms of assistance are available to them.

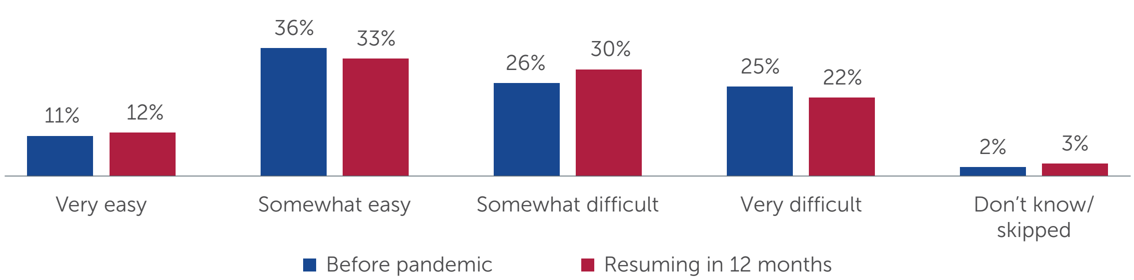
As of 2023, only about a quarter of the borrowers were enrolled in one of the IDR plans (income-contingent, income-based, income-sensitive, Pay As You Earn, or REPAYE).[15] As borrowers transition back into repayment, it is critically important to ensure they all have the tools and information needed to be successful, including an awareness and understanding of their repayment options.

Confidence that some or all of your loans will be forgiven*



**Of survey respondents who reported borrowing student loans*
Source: Trellis Company, Fall 2022 Student Financial Wellness Survey

How easy or difficult was it to afford your student loan payments before the COVID-19 pandemic and how easy or difficult would it be to afford payments if you had to resume payments in 12 months?*



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Federal Policy Recommendations

Enhance loan counseling requirements

Congress should pass a law requiring federal student loan recipients to undergo annual, interactive counseling that provides them with key information like accumulated debt levels, anticipated monthly payments under standard and IDR plans, and projected monthly earnings based on programs of study.

Make it easier for institutions to partner with organizations to offer students additional financial literacy resources

Congress should remove preferred lender list obstacles that are preventing state-based and nonprofit organizations from offering families additional resources on campuses. These public-purpose entities can help students make responsible borrowing decisions and prevent excessive student loan indebtedness.

Simplify the number of repayment plans available to students

Congress should simplify and reduce the numerous student loan repayment plans currently available to decrease confusion and make it easier for borrowers to understand their choices and successfully repay their obligations.

Improve communication with stakeholders to help borrowers transition back to repayment

The Department of Education should leverage the expertise and reach of its partners and other stakeholders to inform borrowers of the rules and procedures they must follow to successfully transition back to repayment.

Use formal channels for guidance

The Department of Education should provide clear and concise guidance through formal means, such as Electronic Announcements and Dear Colleague Letters, rather than through website updates, quotes in news articles, and press releases. This ensures all partners and other stakeholders can give borrowers the same accurate information in a timely manner.

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