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IN FOCUS

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Direct Loan Program Student Loans: Terms and Conditions

The William D. Ford Federal Direct Loan (Direct Loan) program is the single largest source of federal financial aid supporting students' postsecondary educational pursuits. As of June 30, 2022, $1.4 trillion in principal and interest on Direct Loan program loans, borrowed by or on behalf of 37 million individuals, remained outstanding. Upon obtaining a loan, a borrower assumes a contractual obligation to repay the debt over a period of time that may span a decade or more.

Under the program, the government makes loans to individuals using federal capital. Once made, the loans are an asset of the federal government, and the government assumes the risk of losses that may occur as a result of borrower default, loan discharge, or loan forgiveness. The Department of Education's (ED's) Office of Federal Student Aid (FSA) is the primary entity tasked with administering the program. Working with FSA, institutions of higher education originate loans to borrowers, and FSA contractors service and collect on program loans.

This In Focus provides a brief overview of the terms and conditions of loans made under the Direct Loan program. For a comprehensive description of these terms and conditions, see CRS Report R45931, *Federal Student Loans Made Through the William D. Ford Federal Direct Loan Program: Terms and Conditions for Borrowers*. This In Focus does not provide information on student loan flexibilities and debt relief available to borrowers in light of the COVID-19 pandemic. For information on those topics, see CRS Report R46314, *Federal Student Loan Debt Relief in the Context of COVID-19*.

Direct Loan Types

Under the Direct Loan program, four types of loans are available. *Direct Subsidized Loans* are available only to undergraduate students with financial need. *Direct Unsubsidized Loans* are available both to undergraduate and graduate students. *Direct PLUS Loans* are available to graduate students and parents of dependent undergraduate students. *Direct Consolidation Loans* allow borrowers to combine debt from multiple existing federal student loans into a single new loan. The latter three loan types are available to borrowers regardless of financial need.

Eligibility and Amounts That May Be Borrowed

Eligibility to borrow a Direct Loan varies by loan type, borrower characteristics (e.g., dependency status, financial need), program level (e.g., undergraduate or graduate), and class level (e.g., 1st year, 2nd year). The amount an individual may borrow is subject to annual and aggregate borrowing limits (**Table 1**), and federal need analysis and packaging procedures. In general, loans are available in amounts constrained by program rules, regardless of a borrower's ability to repay. Eligibility to borrow a Direct PLUS Loan depends on an individual's creditworthiness.

Table 1. Annual and Aggregate Loan Limits by Borrower Type and Program Level

Borrower Type and Program Level[a]	Annual Limit	Aggregate Limit
Undergraduate Students		
Total Subsidized[b] and Unsubsidized Loans—Dependent Students[c]		
1st year	$5,500	$31,000
2nd year	$6,500	
3rd year and above	$7,500	
Total Subsidized[b] and Unsubsidized Loans—Independent Students[c]		
1st year	$9,500	$57,500
2nd year	$10,500	
3rd year and above	$12,500	
Graduate Students		
Unsubsidized Loans, in general	$20,500	$138,500[d]
PLUS Loans, in general	COA-EFA[e]	Not limited
Parents of Dependent Undergraduate Students		
PLUS Loans, in general	COA-EFA[e]	Not limited

Source: HEA §§428, 428H, 451, and 455; 34 C.F.R. §685.203.

a. Table depicts borrowing limits for undergraduate and graduate educational programs in general. Different annual and aggregate loan limits may apply to specified educational programs, such as preparatory coursework for an undergraduate program or graduate health professions programs.

b. Annual and aggregate limits apply to Direct Subsidized Loans (not displayed in table) and the total combined amount that may be borrowed through Direct Subsidized and Unsubsidized Loans (displayed). Aggregate borrowing limits for Direct Subsidized Loans equal $23,000.

c. In determining Direct Loan eligibility, parents' income and assets are used for dependent students, and the student's income and assets (and their spouse's, if applicable) are used for independent students.

d. Aggregate loan limits for graduate students include amounts borrowed for undergraduate study.

e. There is no statutory borrowing limit for Direct PLUS Loans; however, all estimated financial aid (EFA) may not exceed cost of attendance (COA).

Interest

Interest is charged on Direct Loan program loans. All loans currently being made through the program have fixed interest rates that remain constant from the time the loan is made until it is paid in full. For new loans made during each 12-month period from July 1 through June 30 (with the exception of Direct Consolidation Loans), the applicable interest rate (**Table 2**) is determined by summing: (1) the bond equivalent rate of the 10-year U.S. Treasury notes auctioned at the final auction preceding June 1, and (2) an add-on rate, which varies by loan type and program level for which the loan was borrowed. Interest rate caps apply. For Direct Consolidation Loans, interest rates are determined by calculating the weighted average of the interest rates in effect on the loans being consolidated, and rounding the result to the nearest highest one-eighth of 1%. Interest subsidies are largely limited to Direct Subsidized Loans; however, subsidies may be provided on all loan types in certain cases.

Table 2. Interest Rates on Direct Loans Made July 1, 2022-June 30, 2023

Borrower Type	Subsidized Loan	Unsubsidized Loan	PLUS Loan
Undergraduate students	4.99%	4.99%	n.a.
Graduate students	n.a.	6.54%	7.54%
Parent of dependent undergraduate students	n.a.	n.a.	7.54%

Source: U.S. Department of Education, Office of Federal Student Aid, "Interest Rates for Direct Loans First Disbursed on or After July 1, 2022 and Before July 1, 2023," https://studentaid.gov/understand-aid/types/loans/interest-rates#rates.

Note: n.a.=not available.

Loan Origination Fees

Loan origination fees are charged to borrowers of Direct Subsidized Loans, Direct Unsubsidized Loans, and Direct PLUS Loans; no fees are charged to borrowers of Direct Consolidation Loans. These fees help offset federal loan subsidy costs by passing along some of the costs to borrowers. Origination fees are calculated as a proportion of the loan principal borrowed and are deducted from the loan before it is disbursed to a borrower. The HEA specifies a loan origination fee of 1% for Direct Subsidized and Unsubsidized Loans and of 4% for Direct PLUS Loans. Budget sequestration orders that apply to direct (mandatory) spending may require the origination fee to be increased in a given fiscal year.

Loan Repayment Plans

Numerous repayment plans, each with different payment structures and maximum durations, are available to borrowers. Except for the five income-driven repayment (IDR) plans, all repayment plans require borrowers to make fixed or graduated monthly payments, and monthly payments must cover the interest that accrues. Borrowers must pay off the entire balance of their loan (including interest that accrues) within a maximum timeframe (10-30 years).

The IDR plans cap monthly payments at a specific percentage (10%, 15%, or 20%, depending on the plan) of a borrower's discretionary income. Under these plans, a borrower's monthly payment may be as low as $0. The IDR plans allow for monthly payments to be less than the interest that accrues. Any remaining loan balances after a specified period (e.g., 20 or 25 years) are forgiven.

Deferment and Forbearance

Deferment is a temporary period during which a borrower's obligation to make regular monthly payments on their loan is suspended, and during which an interest subsidy may be provided. Deferments are available for a variety of reasons, such as when a student is pursing postsecondary education, performing military service, or experiencing economic hardship.

Forbearance is a temporary period during which a borrower may cease making monthly payments, make payments in reduced amounts, or make payments over an extended period. In most cases, an interest subsidy is unavailable during forbearance periods. Forbearance is available for a variety of reasons, such as when a borrower is experiencing temporary hardship or during periods when ED is processing certain loan benefits.

Loan Discharge and Loan Forgiveness

A borrower may be relieved of the obligation to repay all or a portion of their loans in certain circumstances. Student loan debt may be discharged on the basis of borrower hardship (e.g., total and permanent disability, bankruptcy, school closure) or may be forgiven following an extended period of repayment according to an IDR plan or completion of a period of public service.

Loan Default

A Direct Loan is considered to be in default once the borrower fails to make payments when due or has otherwise not adhered to the terms of the loan for 270 days. Upon default, the loan balance becomes due in full and the borrower loses eligibility for many borrower benefits (e.g., deferment, forbearance, loan forgiveness), as well as access to other forms of federal student aid. The government uses numerous means to collect on defaulted student loan debt such as administrative wage garnishment and offset of federal income tax returns and Social Security benefits. Options are available for a borrower to bring a defaulted loan back into good standing.

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