

## Promoting Tax-Exempt Financing of Education Loans to Reduce Costs for Students and Families

Since 1976, state-sponsored student loan organizations have been authorized by Congress to issue tax-exempt bonds to provide low-cost loans to students and parents to help them pay for the costs of a postsecondary education. These state and nonprofit organizations originate new private education loans and refinance those with higher rates, thus offering borrowers a competitive interest rate and lower or non-existent origination fees. These organizations also acquire student loans originated by banks, savings and loans, and credit unions, thus allowing those institutions to make additional loans. Tax-exempt financing is critical to these organizations as the loan programs they offer in their respective states support college access and success initiatives and assist struggling borrowers in managing repayment of their loans.

States have taken different approaches to forming nonprofit student loan organizations; some created state agencies or public authorities while others formed nonprofit corporations under general state nonprofit law, subject to additional requirements under the Internal Revenue Code of 1986 (the Code). The latter organizations are typically referred to as “qualified scholarship funding corporations” and must comply with section 150(d), as well as section 501(c)(3), of the Code. Under section 150(d) of the Code, these nonprofit student loan organizations are authorized to issue tax-exempt bonds to finance only student loans made under the federal guaranteed student loan program. Congress eliminated this program in 2010, thus limiting the ability of nonprofit organizations in certain states, including those in Arizona, California, Montana, Tennessee, and Texas, to offer low-cost private education loans.

### NCHER Reform Proposals

The National Council of Higher Education Resources (NCHER) believes tax-exempt private activity bonds provide an important public benefit that needs to be preserved as part of any comprehensive reform of the tax code. We urge Congress to promote the use of tax-exempt financing to assist students, borrowers, and families by:

- Preserving tax-exempt financing of education loans as part of any tax reform package. As tuition costs have outpaced increases in the loan limits authorized under the federal student loan program, the availability of private education loans financed by tax-exempt bonds helps families across the nation “close the gap” in financing their higher education dreams, in many cases at lower rates than are generally available under the federal program. Current law caps the amount of tax-exempt bonds that can be issued in each state to fund student loans, along with certain housing and economic development programs, ensuring that these loan programs are appropriately managed by the states. As Congress begins the effort to reform the nation’s tax code, the ability of state and nonprofit organizations to continue to fund these important private loan programs by issuing tax-exempt bonds is critical and should be preserved.
- Supporting H.R. 480, the “Student Loan Opportunity Act,” allowing 150(d) organizations to access tax-exempt financing for private education loans. When section 150(d) was put into effect, the federal guaranteed student loan program was the major federally-sponsored loan program and there was little need for private loan programs since the cost of tuition was generally in line with the loan limits authorized under the federal program. Since Congress in 2010 eliminated new student loan originations under the guaranteed program, these state-sponsored qualified scholarship funding corporations are now prevented from making lower-cost private education loans available to students and parents. Congress should support H.R. 480, the “Student Loan Opportunity Act,” introduced by Reps. Bill Flores (R-TX) and Henry

Cuellar (D-TX) to update section 150(d) of the Code by striking the limitation to loans made under the old guaranteed student loan program authorized under the Higher Education Act. This simple technical change would allow these organizations to make lower-cost private loans available to students and parents, refinance existing higher interest rate student loans, and expand opportunities and resources for students, borrowers, and families.

The legislation also clarifies that these nonprofit student loan organizations can perform student assistance-related activities defined as offering college access, financial literacy, and outreach programs to borrowers; providing information about student loan programs and higher education finance matters to students and families; handling communications with schools and borrowers; monitoring a student borrower's location and continued enrollment; and engaging in default prevention activities.

- Repealing the Alternative Minimum Tax (AMT), or excluding tax-exempt student loan-based securities from the AMT. As noted above, tax-exempt financing issued by nonprofit student loan providers directly benefits student and parent borrowers through lower interest rates and robust college access and financial literacy programs. However, the income to investors on tax-exempt student loan bonds is subject to the AMT, as these bonds are deemed to be private activity bonds. The AMT adds approximately one-quarter of one percent to a full percentage point to the interest rate of these tax-exempt bonds. This added cost must be passed through to student loan borrowers. Thus, the AMT constitutes a significant barrier to the ability of state and nonprofit student loan organizations to fulfill their missions of assisting students and families access a college education. The Blueprint titled, "A Better Way Forward for Tax Reform," released by House Ways and Means Committee Chairman Kevin Brady in June 2016, calls for the repeal of the AMT. Congress should support this position or, at a minimum, ensure that student loan-based securities are exempted from the AMT as part of any tax reform legislation.
- Clarifying tax-exempt bonds used to make private loans that refinance existing tax-exempt private loans are not advance refunding bonds. In 2015, the Internal Revenue Service (IRS), through the issuance of Notice 2015-78, provided guidance on the rules governing the uses of tax-exempt funds to finance private education loans. While the guidance was welcome, it left some ambiguity that has caused confusion for many issuers and placed restraints on what the private capital markets can offer to student and parent borrowers in the form of lower-borrowing costs to finance their postsecondary education. For example, there is a question of whether the refinancing of an original tax-exempt financed loan causes the bonds to be deemed refunding bonds. If it does, a separate set of restrictive rules would come into play, hamstringing any refinancing program using tax-exempt bonds. Congress should clarify, or direct the IRS to clarify, that tax-exempt bonds issued to refinance an original loan financed with tax-exempt bonds will not be considered advance refunding bonds, particularly where the issuer utilizes new volume cap to issue the bonds that will refinance the original loans.

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